DISCUSSION PAPER

MORTGAGE FORECLOSURE AND SALE

Law Reform Commission of Nova Scotia
July 1997

WHAT DO YOU THINK?

The Law Reform Commission is very interested in knowing what you think about the issues raised in the *Discussion Paper*: *Mortgage Foreclosure and Sale.*

We have attempted, as much as possible, to describe the law and the problems with the present system in a way that can be understood by people who are not lawyers and who are not familiar with the legal system. Your criticism and comments will assist us in preparing a Final Report to the Minister of Justice on how the foreclosure system in Nova Scotia can be reformed.

This Discussion Paper is not a Final Report and it does not represent the final views of the Commission. It is designed to encourage discussion and public participation in the work of the Commission.

If you would like to comment on our suggestions you may:

- Fax a letter to the Commission at (902) 423-0222
- Send an e-mail to lawrefns@fox.nstn.ca
- Telephone the Commission at (902) 423-2633
- Write to the Commission at the following address:

  Foreclosure Project
  Law Reform Commission of Nova Scotia
  2nd Floor, 1484 Carlton Street
  Halifax, Nova Scotia
  B3H 3B7

In order for us to fully consider what you think about these issues before we prepare our Final Report, please contact us by **October 31, 1997**.

Please note that the Final Report will list the names of individuals and groups who make comments or submissions on this Discussion Paper. Unless comments are marked confidential, the Commission will assume respondents agree to the Commission's quoting from or referring to comments made. Respondents should be aware that the Nova Scotia *Freedom of Information and Protection of Privacy Act* may require the Commission to release information contained in submissions.

The Law Reform Commission of Nova Scotia was established in 1991 by the Government of Nova Scotia under an *Act to Establish an Independent Law Reform Commission.*

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MORTGAGE FORECLOSURE AND SALE

SUMMARY

Individuals or businesses buying a house or commercial property often need to borrow money to help pay the purchase price. They usually borrow this money by taking out a "mortgage" with a bank or trust company. A mortgage is a legal agreement (or contract) by which the borrower pledges the property as security for the loan. If the borrower fails to make the payment on the mortgage,[1] the lender may "foreclose" on the property. In foreclosing, the lender takes legal steps to get ownership of the property and the right to sell it to pay off the mortgage. If there is any money still owing after property is sold, the lender may attempt to have the borrower pay the shortfall.[2]

In 1996 the Law Reform Commission began to study mortgage foreclosure law and practice in Nova Scotia. The Commission was responding to concerns that the present system is cumbersome, expensive, inefficient and unfair. There is a perception the system does not work well for homeowners, business people and financial institutions.

The goal of the law of foreclosure and sale is clear: the law must provide some way for the lender to realize on its security where the borrower is in default. This requires a balancing of diverse interests. Borrowers must have reasonable access to credit in order to enable them to purchase property. Lenders, on the other hand, must be able to profitably provide such credit while having access to remedies should the borrower default. At various times and places, the means of achieving this goal has swung in favour of the borrower, and at other times and places, it has favoured the lender.

Current Law and Practice

The current law on foreclosure and sale in Nova Scotia is largely governed not by legislation but by the Civil Procedure Rules and a Practice Memorandum, both issued by the Judges of the Supreme Court of Nova Scotia. Court decisions are also a very important source of law in this area.

Practically speaking, foreclosure and sale is the ultimate and final remedy currently available to lenders in Nova Scotia. While other measures are available, they are only temporary. For example, a lender may "enter into possession" of a property if it has been abandoned by the borrower. Another option is an "assignment of rentals" which permits a lender to collect rents previously paid to the borrower. If the borrower is unable to rectify the default, the lender will eventually seek an order from the court, currently known as an Order for Foreclosure, Sale and

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[1] While there are many types of default, the most common is when the borrower gets behind in making payments. This is the only type of default that will be referred to in this Discussion Paper.

[2] In law, the borrower is referred to as the "mortgagor" and the lender is referred to as the "mortgagee". For purposes of clarity, they will be referred to here as borrower and lender.

Possession.

Once the Order is granted, the sale is advertized and a sale by public auction is conducted by the local Sheriff. Until the property is sold, the borrower may stop the foreclosure process by paying the amount owing. If this does not happen, the Sheriff's sale proceeds. Often, only the lender is present at the Sheriff's sale and there is no competitive bidding for the property. The lender frequently purchases the property and receives a deed from the Sheriff. The lender then attempts to sell the property to a third party in order to use the sale proceeds to pay off the mortgage. If the sale proceeds are not enough to cover the amount owing, the lender may apply to the court for an order requiring the borrower to pay the shortfall, known as the "deficiency". This application must be made within six months from the date of the Sheriff's sale. The application for a deficiency judgment may be refused, granted in full, or granted at a reduced amount.

Perceptions of Current System

It is perceived borrowers are losing their homes and businesses to foreclosure while not able to afford legal advice or be represented by a lawyer in court. This results in virtually all foreclosure applications being undefended and judges having to take on the role of "defence counsel" for the absent borrower. After losing their property, borrowers may also have a judgment against them for any deficiency on the mortgage account (even after crediting the account with the proceeds from selling the property). In Nova Scotia, a judgment is valid for twenty years. When recorded at the Registry of Deeds, a judgment affects a borrower's ability to deal in real property. It usually also affects a borrower's credit rating. Attempts to collect on the judgment can be made throughout the twenty year period. The impact on business people may be somewhat different due to corporate protections and the fact the property is a business asset, not a family asset.

It is perceived lenders are also dissatisfied with the current system. They have to go through a cumbersome, expensive procedure once default occurs. After suing the borrower and obtaining an Order for Foreclosure, Sale and Possession, the property is offered for sale by the Sheriff. Frequently there are no other bidders and no competitive bidding. The lender thus purchases the property at the Sheriff's sale for a nominal price (Sheriff's fees and outstanding property taxes). If the property is a commercial or rental property, property managers are often hired to manage the property and collect rents. Appraisals are conducted to value the property. A real estate agent may be retained and the property offered for sale on the open market. If the property sells, the lender calculates whether a deficiency still exists on the mortgage account after crediting the sale proceeds. If there is a deficiency, the lender may apply to the court for a judgment against the borrower. If the property does not sell, the lender may determine whether a deficiency exists using appraised values as the "resale" value. Once it has a judgment, the lender can attempt to collect the amount owing from the borrower.

Suggestions for Reform

The Commission believes foreclosure law and practice in Nova Scotia is in need of reform. The current system is problematic for both borrowers and lenders. Overall, the system is unfairly balanced in favour of lenders and does not adequately protect borrowers. A primary problem is that Nova Scotia law and practice is not oriented toward achieving the best possible price at a Sheriff's sale. The Commission believes reform of the law of mortgage remedies is necessary and makes the following suggestions:

(i) The Sheriff's sale should be abolished and replaced with a sale on the open market. The court would continue to oversee the process. The Commission is therefore suggesting a modified judicial sale. This new process would make more use of appraisals than the current system and would therefore have to include safeguards regarding the use of appraisals. The Order for Foreclosure, Sale and Possession would take one of two forms, with the court's approval, depending on the value of the property at the time of default (that is, whether there is "equity" in the property):

A **If there is equity in the property** - If the appraisal evidence indicates the property has a value greater than what is owed, a surplus is considered to exist and the property would be listed with a real estate agent for four months.

- **If sold** - A sale of the property could occur at various purchase prices. If the purchase price is greater than the appraised value, the lender would account to the borrower and other subsequent lenders ("encumbrancers") for the surplus. If the purchase price is less than the appraised value but more than the amount owed, the lender would have no choice but to agree to a sale because its debt would be covered. The borrower and others would have to consent to the sale because their claims would likely be compromised by the reduced sale price. If the purchase price was less than the amount owed, the sale could only proceed if the borrower agrees and if the lender and other encumbrancers agree to accept this amount in full satisfaction of the debt.

  A lender could only buy the property with the consent of the borrower. In some cases, this option may be proposed by the parties as the best solution. Any purchase by the lender, at any time, would have to be approved by the court.

- **If not sold** - If the property did not sell, the lender would have two options. The *first option* would be to accept the property in full satisfaction of the debt. There would be no surplus payable to the borrower even though the appraised value is greater than the amount owed. There would also be no surplus if the property later resold at a surplus because it would be inappropriate to require the lender to continue to report to the court indefinitely. Any risk of the lender gaining a surplus may be offset by the borrower having the right to participate in attempts to

market and sell the property. The *second option* would be for the lender to surrender the property to subsequent encumbrancers in order of priority. If each encumbrancer refused to take the property, the property would be returned to the borrower. The lender's recourse would then be to sue the borrower under the covenants in the mortgage for the full amount owing, independent of the property. This right already exists in mortgage agreements and the lender is under no obligation in law to realize on property taken as security for the mortgage.

B **If there is no equity in the property** - If the appraisal evidence indicates the value to be less than what is owed, a deficiency is considered to exist. The lender would have two options. The *first option* is to issue a foreclosure order immediately, thus vesting the equitable title in the lender without further delay. This would ensure the deficiency is not further increased (through interest, property management and other expenses) while the lender attempts to resell the property. The value of the property would be deemed to be the appraised value and the lender would be permitted to apply for a deficiency judgment against the borrower using the appraised value. The *second option* would be similar to that outlined above when there is no equity in the property and no sale has occurred. The lender would surrender the property to subsequent encumbrancers in order of priority. If each encumbrancer refused to take the property, it would be returned to the borrower and the lender could sue the borrower under the covenants in the mortgage.

(ii) In relation to appraisals, the lender would be required to provide the borrower with a copy of the appraisal done at the time of the mortgage. The appraisal prepared for the lender at the time of default would have to be attached to the notice of the court application for the Order for Foreclosure, Sale and Possession. The appraisal would have to be prepared by a company independent of the lender. It would have to explain *any* discrepancy from the appraisal done at the time of the mortgage. All parties, including subsequent encumbrancers, would have an opportunity to review and challenge the lender's appraisal. Challenges could be based not only on other appraisals but on actual offers to purchase the property.

(iii) Reform should include provisions requiring a notice of default to borrowers, written in plain language. Among other things, the notice would outline the rights and obligations of the borrower, the steps necessary to remedy the default and advise that the mortgage can be reinstated by paying arrears and related expenses within a specified time.

(iv) If there is no equity in the property, as outlined under (i) B above, a foreclosure order is issued immediately thus vesting equitable title in the lender. The lender would be permitted to apply for a deficiency judgment against the borrower using the appraised value. The Commission invites further comment on whether this should be permitted and if so, whether the amount of any deficiency judgment should be limited in any way. For

example, should the deficiency judgment be limited to a percentage of the original mortgage loan?

(v) Reform would best be accomplished by legislation and, where necessary, by amendments to the Civil Procedure Rules and Practice Memorandum.

The Commission is seeking advice from the public on these suggestions and on any other issues raised in this Discussion Paper. Once the Commission has received and considered public commentary, a Final Report will be prepared and presented to the Government of Nova Scotia.

SAISIE ET VENTE DE BIENS HYPOTHÉQUÉS

SOMMAIRE[3]

La plupart du temps, lorsque des particuliers et des entreprises décident d'acheter un bien immobilier, ils doivent emprunter afin de payer le prix d'achat. Ils empruntent habituellement ces fonds en contractant un prêt "hypothécaire" auprès d'une banque ou d'une compagnie de fiducie. Une hypothèque constitue un accord juridique (ou contrat) en vertu duquel l'emprunteur nantit le bien immobilier afin de garantir le prêt. Si l'emprunteur manque à son obligation d'effectuer les paiements hypothécaires[4], le prêteur peut saisir le bien immobilier. En saissisant le bien, le prêteur entreprend un processus juridique lui permettant de devenir propriétaire du bien immobilier et d'obtenir le droit de le vendre afin de rembourser le prêt hypothécaire. Si le montant du prêt n'est pas remboursé intégralement après la vente, le prêteur pourra tenter d'obtenir le remboursement du solde de la dette par l'emprunteur.[5]

En 1996, la Commission de réforme du droit de la Nouvelle-Ecosse a commencé à étudier le droit des saisies hypothécaires et son application pratique en Nouvelle-Ecosse. La Commission a entrepris cette action en réponse à l'opinion répandue que le système actuel est lourd, onéreux, inefficace et inéquitable. Selon l'opinion répandue, le système est d'application inappropriée en ce qui concerne les propriétaires de résidences, les gens d'affaires et les institutions financières.

Le but du droit des saisies et ventes hypothécaires est clair: permettre au prêteur de réaliser ses garanties dans un contexte juridique lorsque l'emprunteur manque à ses obligations. Ceci nécessite d'en arriver à équilibrer les divers intérêts en jeux. Les emprunteurs doivent avoir un accès raisonable aux possibilités d'emprunts afin de leur permettre l'achat de biens immobiliers. D'un autre côté, les prêteurs doivent pouvoir financer les emprunteurs de façon rentable tout en conservant des recours lorsque l'emprunteur manque à ses obligations. Selon les époques et les lieux, les moyens permettant d'atteindre ce but ont tantôt favorisé l'emprunteur et tantôt le prêteur.

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[3] Traduit de l'anglais par Me Nathalie Bernard, LL.B (Université Laval), LL.B (Dalhousie University), LL.M (Dalhousie University).

[4] Même si l'emprunteur peut manquer à ses obligations de plusieurs façons, le manquement principal survient lorsque l'emprunteur ne fait pas ses paiements hypothécaires en temps. Le présent *Document de réflexion* ne s'attardera qu'à ce type de manquement.

[5] En droit, l'emprunteur est appelé le "débiteur hypothécaire" (en anglais, "*mortgagor*") et le prêteur, le "créancier hypothécaire" (en anglais, "*mortgagee*"). Afin de simplifier les choses, nous les appelerons "emprunteur" et "prêteur".

Le droit et la pratique actuels

Le droit actuel sur les saisies et ventes hypothécaires en Nouvelle-Ecosse est régit non pas par des lois mais plutôt par les Règles de procédure civile (en anglais, "Civil Procedure Rules") et le Circulaire sur les règles de pratique (en anglais, "Practice Memorandum"), tous deux émanant des juges de la Cour Suprême de la Nouvelle-Ecosse. Les décisions des tribunaux contribuent aussi à l'interprétation du droit dans ce domaine.

En pratique, la saisie et vente hypothécaire constitue le recours ultime et final actuellement offert aux prêteurs en Nouvelle-Ecosse. Alors que d'autres moyens d'actions existent, ils ne sont que temporaires. Par exemple, le prêteur peut "prendre possession" d'un bien immobilier s'il a été abandonné par l'emprunteur. Une autre alternative consiste en la "cession des loyers" laquelle permet au prêteur de percevoir les loyers qui étaient antérieurement payés à l'emprunteur. Si l'emprunteur ne peut remédier au manquement à ses obligations, le prêteur demandera éventuellement au tribunal d'émettre une ordonnance de saisie, de vente et de possession.

Une fois l'ordonnance accordée, la vente est publiée et une vente à l'enchère publique est tenue par le shérif de la région. Avant la vente du bien immobilier, l'emprunteur peut mettre fin au processus de saisie hypothécaire en remboursant la somme due. Si le remboursement n'a pas lieu, la vente par le shérif aura lieu. Il arrive fréquemment que seul le prêteur assiste à la vente par le shérif et qu'il n'y ait pas d'enchères relativement au bien immobilier. Habituellement, le prêteur acquiert le bien immobilier et se fait donner un titre constitutif de propriété par le shérif. Le prêteur tentera par la suite de vendre le bien immobilier à un tiers afin de rembourser le prêt à même le produit de la vente. Si le produit de la vente n'est pas suffisant pour rembourser le prêt, le prêteur peut déposer une requête auprès du tribunal afin que lui soit accordée une ordonnance ordonnant à l'emprunteur de payer le déficit. Cette requête doit être déposée dans les six mois de la date de la vente par le shérif. Le tribunal peut refuser cette requête, l'accorder en entier ou l'accorder pour une somme moindre.

Comment le système actuel est perçu

Sous le système actuel, il appert que les emprunteurs sont dépossédés de leur résidence et commerce suite à la saisie hypothécaire alors qu'ils n'ont pas les moyens d'obtenir les conseils d'un avocat ou d'être représentés par un avocat devant le tribunal. Il en résulte qu'en pratique presque toutes les requêtes en saisie hypothécaire demeurent incontestées et les juges doivent remplir le rôle de "l'avocat défendant les intérêts de l'emprunteur absent". Après avoir été dépossédé, l'emprunteur, le prêteur peut aussi obtenir un jugement contre le prêteur pour le déficit (même après avoir déposé le produit de la vente dans le compte bancaire relatif au prêt). En Nouvelle-Ecosse, un jugement est valide pour vingt ans. Une fois inscrit au Registre des titres constitutifs de propriété (en anglais, "Registry of Deeds"), un jugement affectera la capacité d'un emprunteur de transiger en matière immobilière. Cela aura aussi un impact sur toute évaluation de crédit relative à l'emprunteur. Des mesures de recouvrement en vertu du jugement peuvent être prises tout au long de ces vingt années. L'impact sur les gens d'affaires peut différer quelque peu en raison de la protection résultant de l'entité corporative et du fait que

le bien immobilier est un actif commercial et non familial.

Il appert aussi que les prêteurs sont insatisfaits du système actuel. Dès que l'emprunteur manque à ses obligations, les prêteurs doivent entreprendre une procédure lourde et onéreuse. Après avoir poursuivi l'emprunteur en justice et avoir obtenu une ordonnance de saisie, vente et possession, le bien immobilier est mis en vente par le shérif. Il arrive fréquemment que seul le prêteur assiste à la vente par le shérif et qu'il n'y ait pas d'enchères relativement au bien immobilier. Le prêteur acquiert donc le bien immobilier lors de la vente par le shérif pour une somme nominale (équivalant aux droits payables au shérif et aux taxes foncières impayées). S'il s'agit d'un bien immobilier commercial ou loué à un tiers, les services de gestionnaires doivent fréquemment être engagés afin de gérer le bien et percevoir les loyers. Le bien immobilier sera l'objet d'évaluations foncières . Les services d'un agent d'immeuble pourront être engagés et le bien immobilier mis en vente sur le marché. Si le bien immobilier est vendu, le prêteur calculera si un déficit demeure après avoir versé le produit de la vente au compte du prêt. Si un déficit existe, le prêteur fera une requête auprès du tribunal afin d'obtenir un jugement contre l'emprunteur. Si le bien immobilier n'est pas vendu, le prêteur pourra déterminer si un déficit existe ou non en utilisant la valeur de l'évaluation foncière comme prix de "revente". Une fois en possession d'un jugement, le prêteur peut prendre les mesures nécessaires afin de percevoir la somme due par l'emprunteur.

Suggestions pour une réforme

La Commission est d'avis qu'une réforme du droit et de la pratique des saisies hypothécaires en Nouvelle-Ecosse doit être amorçée. Généralement, le système est inéquitable en ce qu'il favorise les prêteurs et ne protège pas suffisamment les emprunteurs. Le problème fondamental réside en ce que le droit et la pratique en Nouvelle-Ecosse ne visent pas à obtenir le meilleur prix de vente possible lors d'une vente par le shérif. La Commission est d'avis qu'une réforme des recours hypothécaires est essentielle et propose ce qui suit:

(i) La vente par le shérif devrait être abolie et remplacée par une vente sur le marché. Le tribunal continuerait à surveiller les procédures. La Commission suggère donc une vente en justice modifiée. Cette nouvelle procédure encouragerait une utilisation des évaluations foncières plus efficace que sous le système actuel tout en imposant des directives quant à l'utilisation des évaluations foncières. Avec l'autorisation du tribunal, l'ordonnance de saisie, vente et possession pourrait se présenter sous deux formes, selon la valeur du bien immobilier au moment du manquement à ses obligations par l'emprunteur (en d'autres termes, selon que l'emprunteur a pu bâtir un capital (en anglais, "equity") dans le bien immobilier):

A **Si un capital existe relativement au bien immobilier -** Si l'évaluation foncière indique que le bien immobilier possède une valeur supérieure à la dette, il y a surplus et le bien immobilier serait inscrit auprès d'un agent immobilier pour une période de quatre mois.

* **Si le bien immobilier est vendu -** Le bien immobilier pourrait être vendu à différents prix. Si le prix auquel le bien immobilier est vendu est supérieur à la valeur déterminée par l'évaluation foncière, le prêteur devrait rendre compte à l'emprunteur et aux autres créanciers hypothécaires pour le surplus. Si le prix auquel le bien immobilier est vendu est inférieur à la valeur déterminée par l'évaluation foncière mais supérieur à la somme due, le prêteur n'aurait d'autre choix que d'accepter de vendre à ce prix puisque la dette sera payée. L'emprunteur et les autres créanciers hypothécaires devraientdonner leur accord à cette vente car le prix de vente inférieur pourrait compromettre les créances des autres créanciers hypothécaires. Si le prix auquel le bien immobilier est vendu est inférieur à la dette, la vente ne pourrait avoir lieu que si l'emprunteur consent à la vente et que si le prêteur et les autres créanciers hypothécaires acceptent le paiement et déclarent la dette éteinte.

  Un prêteur ne pourrait acquérir le bien immobilier qu'avec le consentement de l'emprunteur. Dans certains cas, cette alternative sera proposée par les parties comme étant la meilleure solution. Toute acquisition par le prêteur, en tout temps, devrait être approuvée par le tribunal.

* **Si le bien immobilier n'est pas vendu -** Si le bien immobilier n'est pas vendu, le prêteur aurait deux choix. *Premièrement*, il pourrait accepter le bien immobilier en paiement de la dette et déclarer la dette éteinte. Aucun surplus ne serait payable à l'emprunteur même si la valeur déterminée par l'évaluation foncière s'avérait supérieure à la somme due. De même, aucun surplus ne serait payable à l'emprunteur même si le bien immobilier est revendu plus tard à profit puisqu'il serait inapproprié d'exiger que le prêteur ait l'obligation d'informer le tribunal indéfiniment. La possibilité que le prêteur puisse obtenir un surplus est compensée par le droit de l'emprunteur de participer à la promotion et à la vente du bien immobilier. *Deuxièmement*, le prêteur pourrait abandonner le bien immobilier aux créanciers hypothécaires subséquents par ordre de priorité. Si chaque créancier hypothécaire subséquent refusait le bien immobilier, le bien immobilier serait remis à l'emprunteur. Le recours du prêteur consisterait alors en une poursuite contre l'emprunteur en vertu des engagements contenus dans l'acte d'hypothèque pour la somme totale due, indépendamment du bien immobilier. Ce droit de poursuite existe déjà dans les documents constitutifs d'hypothèque et le prêteur n'est pas légalement obligé de réaliser la garantie, c'-à-d. le bien immobilier, donnée

B **Si aucun capital existe relativement au bien immobilier -** Si l'évaluation foncière indique que la valeur du bien immobilier est inférieure à la somme due,

un déficit demeure. Le prêteur aurait donc deux alternatives. Selon la *première alternative*, il pourrait se faire accorder une ordonnance de saisie hypothécaire immédiatement. Le droit de propriété en équité (en anglais, "Equitable Title") serait donc assigné sans délai au prêteur. Ceci empêcherait le déficit de s'accroître (en raison de l'intérêt qui continuerait à courir, des coûts de gestion du bien immobilier et des autres coûts) pendant que le prêteur tente de vendre le bien immobilier. La valeur présumée du bien immobilier serait celle déterminée par l'évaluation foncière et le prêteur aurait le droit de faire une requête pour un jugement contre l'emprunteur pour le déficit sur la base de la valeur présumée du bien. La *deuxième alternative* serait similaire à celle décrite ci-dessus alors qu'aucun capital n'existe relativement au bien immobilier et qu'aucun transfert du bien n'ait eu lieu. Le prêteur remettrait le bien immobilier aux créanciers hypothécaires subséquents par ordre de priorité. Si chaque créancier hypothécaire refusait d'accepter le bien immobilier, ce dernier serait remis à l'emprunteur et le prêteur pourrait poursuivre en justice l'emprunteur en vertu des engagements contenus dans l'hypothèque.

(ii) En ce qui concerne les évaluations foncières, le prêteur aurait l'obligation de fournir à l'emprunteur une copie de l'évaluation foncière faite lors de la constitution de l'hypothèque. L'évaluation foncière préparée par le prêteur au moment du manquement à ses obligations par l'emprunteur devrait former une annexe de l'Avis de dépôt d'une requête pour ordonnance de saisie, vente et possession. L'évaluation foncière devrait être faite par une compagnie autre que le prêteur. Cette compagnie devrait expliquer *toute* différence entre l'évaluation foncière faite au moment de la constitution de l'hypothèque et celle préparée au moment du manquement à ses obligations par l'emprunteur. Toutes les parties, incluant les créanciers hypothécaires subséquents pourraient prendre connaissance et contester l'évaluation foncière préparée par le prêteur. Les contestations devraient être fondées non seulement sur d'autres évaluations foncières mais aussi sur des offres réelles faites relativement au bien immobilier.

(iii) La réforme devrait comprendre des dispositions prévoyant un avis de défaut à l'attention des emprunteurs, rédigé en termes simples. Entre autres choses, l'avis de défaut énumérerait les droits et obligations de l'emprunteur, les mesures à prendre afin de remédier au manquement et notifierait l'emprunteur que le prêt hypothécaire pourrait être remis en force par le paiement des arriérés et des coûts afférents dans un délai précis.

(iv) S'il n'existe aucun capital dans le bien immobilier, tel qu'expliqué au point (i) B ci-dessus, une ordonnance de saisie hypothécaire est accordée immédiatement, assignant le droit de propriété en équité au prêteur. Le prêteur aurait le droit de déposer une requête pour un jugement contre l'emprunteur pour le déficit sur la base de la valeur déterminée par l'évaluation foncière. La Commission invite le public à lui faire part de son opinion à savoir si le scénario précédemment décrit devrait être permis et dans l'affirmative, si le jugement pour le déficit devrait être plafonné. Par exemple, le jugement pour le déficit devrait-il être limité à un pourcentage du prêt hypothécaire initial?

(v) La réforme devrait être accomplie par voie législative et lorsqu'approprié, par des amendements aux Règles de procédure civile (en anglais, "Civil Procedure Rules") et au Circulaire sur les règles de pratique (en anglais, "Practice Memorandum").

La Commission invite le public à lui faire part de son opinion sur les suggestions faites par la Commission et sur tout autre point soulevé dans ce *Document de réflexion*. Dès que la Commission aura reçu et pris connaissance des commentaires du public, elle préparera un *Rapport final* et le présentera au gouvernement de la Nouvelle-Ecosse.

KI'KK KISNA KUTMOTAQN KOQA'TUKSIN TIJIW MINUI NTUI'SKASIK

SUMMARY

Tan tijiw ki'l kisna pisnissl pekwatelmoq wenjikuoml kisna pisnissewie'wten maqaqmikal, sipeliw nuta'q maqatuin suliewey tan tli apankittesk te'lmuksin. Apjiw na ula teli emqatuin telui'tmik "Mortgage" emqatui'sk pank kisna Trust Company. "Mortgage " na Klusuaqn eywasik. Kil na elui'tmasin wsuatasin ki'kk kis na kutmotaqn, epatkwimaqatuin, tan tijiw mu kisi apaji apankitmu'n tetuo'qn ika'q[6] Aqq amsami meso'tmin apakitmin tetuo'qn kisi ko'qatultew tan wen maqatui'ket[7] Kisi ko'qatultew msit ta'n apatkwi maqatuin', tan tujiw ko'qatask nuji maqatuiket kutmotaqn. Tplutaqniktuk, ujimsntew nekem kisi apaji ika'tasin wtuisnmk, klaman kisi kiwaskipukuasitew aqq ntui'sketew ujit tan petepawtik me ki'l tetuen. Aqq mu msnmuk tan tel tepawtik, na ki'l ujapsknultew eskwi tetuek.

1996 ek a Law Reform Kmissn poqji iloqaptik ko'qaluemkewey tplutaqn Nopa Sko'sia. Kmissn asite'tkis tesik mu koqatenuk systmiktuk, amsami mko'tikiss, kekwe'ksip aqq mu koqaji maliaptasinusip aqq mu tetpie'y asotasinuk. Teli ankamkuk system mu welukwenuk wujit tanik alsutmi'titl wikwal, aqq pissnissl, aqq tanik nuji maqatuikètite'wk.

Tplutaqaniktuk koqa'luemkewey aqq netui'skemkewey wel nsitasimk. Tplutaqn miamuj pantenk tan maqatui'ketewul tli apankituaten tan tijiw emqatuite'wl mu kis apankitmuilij. Na na wula miamuj ilkwenkjik tan tijiw awnasiaq koqowey. Emqatuwultitewk tel tek kisi maqatuin, klaman kisi kpkwatelto tan pewat. Maqatuikete'wk elt kisi uji kisi kanie'win tel maqatui'kej aq kuknmin tan tli msntew tan te'tuj wte'jk eliej emqatuite'wul. Ekkl na'kwekl me aji wela'sik koqowey ujit emqatuite'w, aq ekkl na'kwekl me aji wela'sik ujit maqatui'kete'w.

NIKEY KTPLUTAQN TELI E'WASIK

Nikey tplutaqn maliaptik koqa'luek aqq ntui'skewey, mu legislation mali aptmuk, awnaqa Civil Procedure Rules and a Practice Memorandum, l'pa jaja'q wetaqne'wasultijik Supreme Court of Nopa Sko'sia maliaptimi'tij.

Pa nuku' teluemk, koqa'luek aqq ntui'skewey pasik etek tan elapultitij maqatui'kaqatite'wk Nopa Sko'sia. Ey'kl pilue'l tan kisi lapatimkl pasik kelemuekl. Kutey nikey, maqatui' taqatite'wk kisi alsusite'lsultitaq nqatmin kutmo'taqn tetuek. Ap ktik kisi tla'taqatitaq maqatui'kaqatite'wk, na usua'taq rentl wejkuaqamultimtip. Emqatuwultite'wk mu tepijiknm'n tijiw telitpie'tij klapis na amuj maqatui'kaqatite'wk eli tasuatmiti

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[6] Tlia' pa milamu'kl tel satesinn, mawi sipeliw wula nuji maqatuitt wtejk elaqlsit tan tijiw mu tepjiknmuk tetuo'qnn. Wula tan wtejk elaqlsin pasik eywasitew wula wi'kattkniktuk.

[7] Kplutaqn, telui'tatl emqatui'te'lwl "Mortgagor" aqq maqatui'kete'w "Mortgagee". Wujit me nsitasin, tlui'taten "Maqatuite'w"(Borrower) aqq "Maqatui'kete'w" "Lender".

Koqaluemkewey Aqq Ntui'skewey

Newt sapatekek teli msimuksin, na se'a'sik klusuaqn, ntui'skewey wenaqiaq aqq sheriff nujo'tew salitey. Emqatuwultite'wk kisi naqa'taq ntui'skewey, apankitmitij tan tetue'tij. Mu kisi apankitmi'tiwk na siawatasik salitey. Sipeliw pasik nuji maqatui'kaqatite'wk. asite'lmuji i'minow wula salitey. Maqatui'kaqatite'wk apjiw apatelmitij tan netui'skasik aq mesnmitij wikatikn alsutaqaney. Na nuku maqatui'kaqatite'wk wjo'taq minui ntui'sketminow, wuji tepteminow tan te'ttup. Mu tepte'mitik tetuek, kortiktuk ap ll'tataq aq utiteskitaq emqatuwultite'wk apankitminow eskwi tettuek, kekkunmitij asukom tepknusetk wejatekemk kisi saliteiek. Saputeteskmitij kortiktuk a, jiptuk alu'etaq, kisna iknmuaten tel tawtitij, kisna me aji apje'jk msntaq.

TELIKWSUATIMK NEKEY SYSTEM

Teli ksua'tasik emqatawultite'wk koqkwa'lujik, toqo mu tepawtukew'tiki lawyera' aqq mu tepi nsitmuti'kw tplutaqaniktuk. Mawi tlitpiaq mu eymutitiwk emqatuwultite'wk cortiktuk, na miamuj ja'jj lawyerewiet ujit nekmow. Ki's na koqa'tasik wtmotaqnmuow ap na jijuaqa mu kejitu'tik me tetua'tisnik. Nopa sko'sia tapuiskekipunqik pemanis tetuo'qn. Newt mesqnwi'kasik Registry of Deeds. Maqtewwikasin aqq mu mesnmu'n emqatu'ksin tami se'kk, ewle'juinuin. Katu milesuinu'k piluey tan ikalkwitij.

Teli wsuatasik maqatuitaqatite'wk mu weltetmi'tik system. Newt ika'q poqji nntutij suliewey, piamikeskatite'tmitij tan amuj telataqatijik wekow apato'sultitij.

ILUTASIK I'LJO'QTAQN

Nopa Sko'sia tplutaqn nuji maliaptik koqa'ltimkewey aqq ntui'skewey nuta'q iloqaptasin. Kitnimtijik tanik ewmitij wula system. Me aji ikalaji maqatuitaqatite'wk je mu emqatuwultite'wk. Etli tetasik Nopa Sko'siaewey ktplutaqn mu asite'tmin tlawtukwen teli ksatmin saliey.

Kmisn ketlamsit iljo'qa'taqn nuta'q aqq ilsutaqnn elmi wikasikl.

(i) Sheriff's Salitey puni e'wasiss, tuju menaqaj ntuiskewey ika'tasiss katu me cortiktuk wtutaqne'wasis.

A **PEKWATIKEK KUTMOTAQN** - Kisi mawkijasi me attepawtin kumotaqn aq tan telikska'task, na tujiw wpitnk lian tan wen nuji ntui'sketoql wenjikuoml aqq tlankuatasin nate'l mi'soqo ne'w tepknusetk.

- **NTUI'SKASIK** - Kisi milawtitew sulieywey wejiaq ntui'skewe'ktuk. Aji mko'tik wejiaq aqq tan tel tepawtik tetuek, emqatuikete'wk miamuj kekinua'tuaji emqatuwultite'wk aq tani (apatkwi emqatui'kete'wk) tan tujiw piamiaq suliewey. Katu aji anawtik ika'q aqq tan tel mawkijasik

katu me atawtik aqq tan tel tetuek, ma kis piam talataqati'kw pasik emqatui'qati'te'kw wije'wminow telitpiaq muta tepiatew tan nekmo tetuj. Emqatuwultite'wk aq ktiki'kk miamuj wulte'taq muta etukje etoqotesultitaq aji anawtik ika'q. I'pa na aji anawtikis ika'q, emqatuite'kw kisi naqa'taq ntui'skewey, misoqo tan emqatui'taqatite'wk wulte'tmino wsua'tunew tan ika'q aq tlu'weno kaqapankituksie'k.

Emqatui'kete'w pasik kisi kpkwateltow ntui'skaqn wulte'tmlij emqatui'te'wul. Miamuj cortiktuk uji Sapa'sitew, emqatui'kete'w kisi kpkwatelmin tan netui'skasik.

- **MU NTUI'SKSINUK** - Mu kis ankuetasitnuk, tapunemi'k tan kis tla'teket emqatui'kete'w. Amskwesewey kis tlatekemk na pasik apaji wsua'toq taqkoqowey wettelasikip emqatui'kejek. Aq ma wja'tuk emqatu'te'w, keskijasik tlia aji anawtik tetuej, aqq elt ma piamiaq tenuk. Ntui'skewey elmiaq minui ntui'skeweyik

Muta mu weli ankamkutnuk asu'teskmin emqatui'kete'w cortiktuk. Mu kisi piami msiki'tnuk piamaqq muta mu alsutmuk emqatui'kete'w tan pasik tli ntui'sken. Tapuowey kis tla'taqantiten naqa emqatui'kete'w ikatuan wpitnuaq tani patkwi emqatui'taqatipnik. Mu wen tesi'tij mnuekek, apaji iknmuksin emqatui'tew. Na nuku' pasik emqatui'ketew su'owalatal emqatui'tewal wujit suliewey. Katu mu wtmotan lukwaqnatuaq. Ki's ula tplutaqn etek wujit apoqnmuan emqatui'qatite'kw.

B **MU ANKUATASITNUK KUTMUTAQN** - Nemitasik mu koqowey piley ankuatasitnuk kutmotaqnk, toqo me attawtik tetuen aqq tan tel petawtik kutmotaqn, na simtuk kisi koqa'lulten. Klaman ma atki'kk tetuewun.

(ii) Emqatui'kete'w miamuj muskatuatl emqatui'te'wal wikatikn tan kiaskiw pettepawtik taqkoqowey ketu kpkwatelk, tan tujiw emqatui'lij. Elmiaq metue'k ikajj emqatui'te'w miamuj wiaqtetew wikatikn kiaskiw pettepawtikip, tan tujiw cortiktuk elaluj emqatui'te'w. Miamuj piluey natuen iloqaptitew tan ketu kpkwatelmin, ma kisi i'ka'lsik tan wen emqatui'ket. Miamuj kinuateketow wejitoq pilu'ten tan pettepawtik tan tesit wenl emqatui'tew tettuatl, kekkunk klusa'sin aq e'tmuan emqatui'kete'wl.

(iii) Il'muekituk tepawtis wiaqten wen emqatuite'w wi'kkmuksin wikatiken tan weli nsitk, kinua'tuskin tan tujiw wtejk poqji mamun liej tettuoqnmk. Aq emqatui'kaqatite'w iknemanow emqatui'te'wl, wujo'timin kis apankitmin tan tetteuj, pas mu pitaqnuk tan tli eskamatew emqatui'kete'w.

(iv) Mu ankuatasitnuk kumotaqn steke'y teluiek (1) B, Simtuk kisi koqalulten kutmotaqn, kisi namkm maliamaten emqatui'kete'w, ma piami ntuk wsulieweyim. Asite'lmaten emqatui'kete'w namkm msimulin aq tluen tettaj pettepawtik wijey aq appraisel. Kmissn pipanikesit asite'tasin ula kis wikasik, aq wultetasin deficiency judgement pasik so much kisi atawtin aqq tan emqatui'tip.

(v) Reform na wul lukwes legislationiktuk wututaqtek, aqq me nuta'w ila'tasin Civil Procedure Rules aqq Practice Memorandum.

Kmisn k'satss mimajuinu kinuataqkuno tan telte'tmi'tij taqkoqowey kisi wsku'tasik wula Discussion Paper. Newt kmisn wtis'tmaj mimajuinu aqq tan telimkwi'ti'ji, Final Report kiskajatasitew aqq iknmuaten kaplnu'l Nopa Sco'siaewa'j.

I INTRODUCTION

1. The mortgage foreclosure project

In response to concerns that the present system is cumbersome, expensive, inefficient and unfair, the Law Reform Commission began to study Nova Scotia mortgage foreclosure law and practice in 1996. The Commission researched the law and practice in Nova Scotia and elsewhere and consulted with various individuals involved in the foreclosure system[8]. In addition, the Commission conducted an empirical study of foreclosure files in the Halifax County Sheriff's Office over a 2 ½ year period. The purpose of this study was to gather information on how the foreclosure process is working in Nova Scotia. Items studied included: the time it took to have a foreclosure sale once the lender sued the borrower; whether the property was purchased at the Sheriff's sale by the lender or a third party; and whether sale prices covered the amount owing on the mortgage. For reasons outlined below, the Commission concluded the current foreclosure system is not working well.

A "mortgage" is taken out by individuals or businesses who wish to buy homes or commercial property but need extra money to help pay the purchase price. They usually borrow the money from a bank or trust company. The party borrowing the money is known in law as "mortgagor" but will be referred to here as the "borrower". The party lending the money is known as "mortgagee" but will be referred to here as the "lender".

The borrower and lender enter into a legal agreement known as a "mortgage". In exchange for the lender providing money to the borrower to buy the property, the borrower pledges the money as security for the loan. If the borrower does not make the payments under the mortgage, the lender may "foreclose" on the property. This means the lender takes steps to get ownership of the property. In Nova Scotia, the lender also gets the right to sell the property and use the sale proceeds to pay off the mortgage. The property is sold by the local Sheriff acting under an order of the Supreme Court of Nova Scotia.

Part II of this Paper contains an overview of foreclosure law and practice including its historical development in Nova Scotia, the law and practice in Nova Scotia, the law in other Canadian jurisdictions and the results of the Commission's empirical study of foreclosure files. In Part III, the Commission considers whether reform is necessary. After concluding that reform is required, the Commission's suggestions for reform are outlined.

A Final Report to the Minister of Justice will be prepared after the Commission has received public comments on this Paper and on the Commission's suggestions for reform.

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[8] The Commission is limiting its review to foreclosure as being the primary and final remedy available to a lender when a borrower defaults in making payments on a mortgage loan. Only provincial legislation is reviewed. Subjects falling within federal jurisdiction, such as loans granted to band councils for construction of housing on reserves, are beyond the scope of this Discussion Paper.

2. Language

This Discussion Paper attempts to present legal information as clearly as possible so that people who do not have legal training can understand and provide comments on the Commission's suggestions for reform. There are still some situations where the language relates to specific legal and technical concepts and the words used will not be familiar to everyone. This section provides definitions of words used in this Discussion Paper.

Act - Law made by elected members of the legislature or parliament. Also referred to as "statutes" or "legislation" and includes regulations.

Arrears - Payments that are due but have not been paid.

Appraisal - A written estimate of the value of a property.

Borrower - The party borrowing money to help pay the purchase price of a property. The borrower is known in law as the mortgagor.

Common law - A body of law developed over the years by judges when making decisions in court. These decisions are relied upon by other judges in making decisions in other cases.

Convey - To transfer title to property.

Covenant - Agreements or promises contained in a mortgage.

Default - Occurs when a borrower fails to do something it is required to do under the mortgage. The most common type of default is failure to make payments.

Deficiency judgment - A judgment applied for by the lender, as against the borrower, when the amount owing under a mortgage (plus costs) is not paid in full by the funds realized from selling the property.

Encumbrance - A claim attached to property. Includes mortgages and other charges such as liens and judgments.

Equity of redemption - A borrower's interest in property that is subject to a mortgage. The borrower has a right to regain full title to the property by paying the amount owing under the mortgage.

Foreclosure - Occurs when the borrower does not make payments under the mortgage (or defaults in some other way) and the lender takes steps to get ownership of the property.

Foreclosure and sale - Occurs when the lender not only forecloses on the property but also gets the right to sell the property and use the sale proceeds to pay off a mortgage debt.

Law of Equity - A body of law which developed to relieve the harshness of the common law. It is seen as a more just or fair type of law. It provides solutions not normally available under the common law.

Legislation - Law made by elected members of the legislature or parliament. Also referred to as "statutes" or "acts" and includes regulations.

Lender - The party lending money to help the purchaser pay the purchase price of a property. The lender is known in law as the mortgagee.

Mortgage - A legal agreement or contract by which a borrower pledges property as security for a loan.

Mortgagee - The party lending money to help the purchaser pay the purchase price of a property.

Mortgagor - The party borrowing money to help pay the purchase price of a property.

Right to redeem - The right of the borrower to regain full legal title to property after paying the amount owing under a mortgage.

Statute - Law made by elected members of the legislature or parliament. Also referred to as "legislation" or "acts" and includes regulations.

Security - Property pledged under a mortgage to ensure the borrower will not default. If default occurs, the lender can take steps to get ownership of the property.

Sheriff - An official appointed by the government who has numerous duties, including conducting public auctions of foreclosed property.

Sheriff's sale - A public auction of property conducted by a Sheriff, acting under the authority of the court, in order to use the sale proceeds to pay off a mortgage debt.

II FORECLOSURE LAW AND PRACTICE

1. The English and Irish influence in Nova Scotia

Common Law and Equity

There are various sources of law. One primary source is "legislation" developed by our governments. Another source is the "common law". This is a body of law developed over the years by judges when making decisions in court. These decisions are relied upon by other judges in making decisions in other cases. The system of common law may be seen as somewhat rigid as it relies upon previously decided cases ("precedents") without much room for deviation. Another source of law is "equity". It is seen as a more just or fair type of law. It provides for solutions which would not normally be available under the common law and therefore avoids the harshness that may result from the common law.

Historically, both the common law and equity have been applied to foreclosure. The two systems, however, viewed a mortgage differently. Under the common law, the borrower's obligations were viewed very seriously. A borrower who did not make payments by the date indicated in the mortgage would lose the property. Once payments were late, the borrower would not be able to regain title by paying the amount outstanding on the mortgage. The lender would retain title and become absolute owner of the property. As a result, the borrower would lose any value built up in the property. This was seen as a rather harsh result.

Equity provided a more just solution. Equity viewed a mortgage as a security arrangement to which the conveyance of legal title was secondary. The lender's principal claim related to payment of the debt. As a result, equity imposed restrictions on the lender's right to seize title to the property once the borrower failed to make payments. If the borrower could show the loan would be repaid within a reasonable period of time, the borrower was given another chance. By making the payments owing, the borrower regained title to the property even though the time set out in the mortgage for making payment had passed. The borrower was recognized as having the *right to redeem* title to the property. The borrower's interest became known as the *equity of redemption*.

Once it became standard practice for borrowers to have extra time to redeem, it was necessary for lenders to have a remedy in case the borrower was unable to pay the outstanding amounts even with the benefit of extra time. This was called *foreclosure*. It resulted in the borrower's right to redeem being forever erased, or foreclosed, once certain conditions were met. Upon default, a borrower could file a bill of foreclosure in the equitable court. The court would then set a final date for payment, usually six months from the date of the order. This would be contained in an order known as a decree *nisi*, a kind of conditional judgment. If payment was not made by the date set by the court, the lender could apply for a final order known as a decree *absolute* of foreclosure. After this point, equity would not intervene again to assist the borrower. The lender was then entitled to be treated as the absolute owner of the property, free of any interest of the borrower.

In Ireland and England, the common law and equity were originally administered by two separate courts. This system was adopted in Nova Scotia with the court of common law being the Supreme Court of Nova Scotia and the court of equity being the Court of Chancery. In 1855, the Court of Chancery ceased to exist as a separate court in Nova Scotia. The principles it applied, however, had become part of Nova Scotia law and continue to be applied by the Supreme Court of Nova Scotia.

English and Irish Practice[9]

In England initially, foreclosure existed on its own, without any provision for a sale of the property. If the borrower failed to make the payments by the date set by the court, the lender simply foreclosed and became the full owner of the property. The mortgage debt was not, however, extinguished by the foreclosure. If the lender tried to claim any balance owing after the foreclosure, it would not be permitted unless the lender was prepared to reopen the foreclosure and give the borrower another chance to redeem. This was consistent with equity's view that the land had simply been pledged and it was unjust to allow the lender to keep the subject of the pledge *and* recover the full debt.

In 1852 the *Chancery Procedure Act* was enacted. It introduced the concept of a sale to foreclosure proceedings in that it gave the English Court of Chancery the authority to order sale of the property. The law still did not, however, permit the lender to bid at an auction or acquire the property through an intermediary.

The Irish system involved both foreclosure *and* sale. When the borrower defaulted, the Irish court would issue an order *nisi* (again, a kind of conditional judgment) for sale and foreclosure. If the borrower did not pay the amount owing by the date set, the court would order the property to be sold at public auction by the Sheriff. As in England after 1852, the lender was not permitted to bid at the auction or acquire the property through an intermediary. Unlike in England, the lender could, without reopening the foreclosure, sue for any balance owing on the mortgage. The court did not require the foreclosure be reopened because the property would have been sold to a third party. The Irish lender had therefore not simply accepted the property in full satisfaction of the debt and could pursue the borrower for any outstanding balance on the mortgage account.

Impact on Nova Scotia Practice

After the founding of Halifax in 1749, the English approach to foreclosure was followed. Orders were granted for foreclosure only. Almost 30 years later, however, the court began to grant orders of foreclosure *and* sale, consistent with Irish practice. There is no indication as to why

[9] See especially W.A. Richardson, "The Irish Mortgage in Nova Scotia" (1991) 17 Nova Scotia Law News 154.

the process changed. There was no law passed requiring such a change and there were no changes to the rules of court. It is noteworthy that virtually all the principal legal officials at the time had Irish backgrounds. Whatever the reason, it appears the practice of granting orders for foreclosure *and* sale became quickly entrenched in Nova Scotia. It has been followed ever since.

Originally, the property was sold by a Master in Chancery, not by a Sheriff. This changed in 1855, when the Court of Chancery was abolished. From that point forward, a Sheriff conducted the sales under the authority of the Supreme Court of Nova Scotia.

Nova Scotia practice began to diverge from both the English and Irish systems in the late 1700s when lenders were permitted to acquire the property at the Sheriff's sale. Again, it appears no law was passed authorizing this practice. Competitive bidding, however, seems to have occurred at the sales because a surplus frequently remained after payment of the mortgage debt and costs. It was not until almost a century later that the courts commented on the practice of the lender bidding at the Sheriff's sale. In *Kenny* v. *Chisholm,*[10] the lender applied for a deficiency judgment after purchasing the property at the Sheriff's sale and conveying it to a third party. The court granted the application, thus allowing the lender to acquire the property *and* sue for a deficiency on the mortgage account. One of the judges doubted whether permitting the lender to purchase the property was legal.[11] In response, the government passed legislation declaring it legal for the lender to purchase the property at the Sheriff's sale.[12]

It has been said that "Nova Scotia has ended up with *both* the Irish and English systems".[13] This has resulted in Nova Scotia having a foreclosure practice which is distinctive in Canada although it is similar to that which exists in some areas of the United States.[14]

It remains the law in Nova Scotia today that the lender may acquire the property at the Sheriff's sale and also apply for a judgment for any deficiency on the mortgage account.

2. Law and practice in Nova Scotia

Legislation

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[10] (1883), 19 N.S.R. 497 (S.C.).

[11] *Ibid.* at 504 (Justice Weatherbe).

[12] *An Act to Confirm Sales of Land under Order of Supreme or Equity Courts*, S.N.S. 1885, c.31, s.3. Section 19 of the *Real Property Act*, R.S.N.S. 1989, c.385, allows "any of the parties" to purchase at the sale, unless the Court or a judge otherwise orders. See Richardson, s*upra* note 9 at 204.

[13] Richardson, *supra* note 9 at 206.

[14] See generally, S. Wechsler, "Through the Looking Glass: Foreclosure by Sale as *de facto* Strict Foreclosure - An Empirical Study of Mortgage Foreclosure and Subsequent Resale" (1985) 70 Cornell L.R. 850.

There are various pieces of legislation in Nova Scotia relevant to foreclosure and sale and mortgage transactions.[15] One of the most significant is the *Judicature Act.*[16] Section 42 permits a borrower who defaults to make an application to the court to discontinue proceedings commenced by the lender. Standard mortgage documents permit a lender to require that a borrower pay the full amount owing under the mortgage, even if only one payment is missed. Section 42 permits the mortgage to be reinstated.[17] This reflects the "second chance" given by the law of equity to a borrower who missed payments but could make them up within a reasonable period of time. Under Section 42, the court may grant an Order of Discontinuance conditional upon the borrower paying all arrears and performing the covenant in default. The court also has authority to order the borrower to pay any costs and expenses incurred by the lender. Subsection (4) allows the court to grant only one Order of Discontinuance for each mortgage. Presumably this is to deal with repeat defaulters and the potential for abuse by borrowers.

Sections 15 to 27 of the *Real Property Act*[18] deal with "Sales by the Court". Section 15 indicates the Supreme Court has power to order sale of real property in all cases in which a court in England had the power to do so. Section 16 provides for land to be sold by the Sheriff "unless the Court or a judge otherwise orders". In Nova Scotia, sales are conducted by the Sheriff and this is confirmed in the Civil Procedure Rules and Practice Memorandum No. 13.[19] There is no requirement in law, however, that the Sheriff be the one conducting the sale.[20]

Section 19 of the *Real Property Act* states that any of the parties to the action may purchase the land at the sale "unless the Court or judge otherwise orders". This clearly confirms the right of the lender to purchase property at a Sheriff's sale. It appears this right has its origin in *An Act to Confirm Sales of Land under Order of Supreme or Equity Courts.*[21] In 1890 the predecessor to Section 19 was inserted in the *Real Property Act*.[22] This allows the court some latitude and may be seen as preserving the court's equitable jurisdiction to supervise the sale of land under its

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[15] Other legislation may also be relevant but is not reviewed here. See, for example, the *Condominium Act*, R.S.N.S., 1989, c. 85, the *Residential Tenancies Act*, R.S.N.S. 1989, c. 401, and the *Land Actions Venue Act*, R.S.N.S. 1989, c. 247.

[16] R.S.N.S. 1989, c. 240.

[17] Not to be confused with the borrower's right to redeem full title to the property before the Sheriff's sale by paying the *full* amount due under the mortgage (as opposed to just paying outstanding arrears). See C.W. MacIntosh, *Nova Scotia Real Property Practice Manual* (Toronto: Butterworths, 1988) at 12-86 to 12-87.

[18] R.S.N.S. 1989, c. 385.

[19] Discussed more fully in the following two sections.

[20] Richardson, *supra* note 9 at 206.

[21] S.N.S. 1885, c. 31.

[22] S.N.S. 1890, c. 14, s.8. See also Richardson, *supra* note 9 at 204.

orders.[23]

The *Matrimonial Property Act*[24] also contains provisions dealing with mortgages. Section 8 lists restrictions on a spouse's right to encumber matrimonial property. For example, one spouse could not put a mortgage on the matrimonial home without the other spouse's consent (unless it was authorized by court order or by a separation agreement or marriage contract). Section 9 indicates that a spouse with a right of possession of the matrimonial home has the same right to redeem as the other spouse and is entitled to any notice of enforcement to which the other spouse is entitled. A lender wishing to foreclose would therefore have to give notice to both spouses and allow them both an opportunity to pay arrears and stop the foreclosure.

Among other things, the *Conveyancing Act*[25] sets out wording which can be used in mortgage clauses. It includes both short and long forms of these clauses. If used in a mortgage agreement, the short form is taken to have the same meaning as the long form.

The *Registry Act*[26] provides for registration of instruments affecting land. In Nova Scotia, they are to be registered in the Registry of Deeds of the district in which the lands are located. There are eighteen registration districts in Nova Scotia. To find mortgages registered against a particular property, one would have to search the Registry of Deeds for the registration district in which the land is located. If one does not know the location of the land but wishes to find mortgages taken out by a borrower, all registration districts may have to be searched.

Section 44 of the *Registry Act* provides for registration of releases of mortgages. A release of mortgage is provided by a lender once a borrower pays the amount owing under a mortgage. Registration of the release indicates the borrower has met all the conditions of the mortgage and the lender no longer has an interest in the property. Section 44(2) of the *Act* provides for cross referencing in that once a release is registered, it must be noted on the mortgage document.

The *Mortgage Brokers' and Lenders' Registration Act*[27] provides for registration of "mortgage brokers"[28]. Section 23 requires a mortgage to indicate whether it can be prepaid. If the mortgage

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[23] Richardson, *supra* note 9 at 204.

[24] R.S.N.S. 1989, c. 275. See also sections 9 and 10 of the draft *Domestic Property Division Act* contained in the Law Reform Commission of Nova Scotia's *Final Report on Reform of the Law Dealing with Matrimonial Property in Nova Scotia*, March 1997.

[25] R.S.N.S. 1989, c. 97.

[26] R.S.N.S. 1989, c. 392.

[27] R.S.N.S. 1989, c. 291.

[28] Defined by s.2(c) of the *Act* as a person who "carries on the business of dealing in mortgages" or of "lending money on the security of real estate" or one who holds himself out as in the business of dealing in mortgages.

is silent, it can be prepaid without penalty at any time.[29] Section 24 requires a lender to transfer a mortgage to a third person if the borrower pays the outstanding balance and does not wish to have a release of mortgage. It is perceived the *Act* is of little value largely because it does not regulate banks and only applies to trust companies, credit unions, and loan companies. Banks are under federal jurisdiction and are thus not considered to be covered by the *Act*.

Civil Procedure Rules

The foreclosure process in Nova Scotia is largely governed by the Nova Scotia Civil Procedure Rules.[30] The Rules are supplemented by "Practice Memoranda and Directions" which provide guidance and direction to lawyers and others using the Supreme Court.

Civil Procedure Rules 12 and 47 are particularly relevant to foreclosure[31]. These Rules were amended effective September 1, 1995. Rule 12.04 allows a lender to apply to the court for an Order for Foreclosure, Sale and Possession after the borrower has been sued (by a document known as an Originating Notice). The lender applies for the right to take ownership of the property and to sell it to pay off the mortgage. The lender must show that the Originating Notice has been served on the borrower and the borrower has not filed a defence in the time period provided (usually 10 days). The lender must provide a certificate showing all encumbrances registered against the land from the date the borrower became owner. The lender must also provide a detailed statement of account showing all payments made on the mortgage, as well as all interest and other charges. If the court is satisfied the lender has done everything it is required to do, the court may order a sale of the property.

Rule 47 deals with sales by the court. Rules 47.08 to 47.13 deal specifically with foreclosure, sale and possession. When a court orders a sale under Rule 12.04, Rule 47.08 directs that the property be sold by the Sheriff of the county in which the lands are located. It also authorizes the Sheriff to provide a deed of the property to the purchaser (known as a "Sheriff's Deed"). Rule 47.08(4) was revised in 1995 to direct the Sheriff to conduct the sale in accordance with the standard procedure set out in a "Practice Memorandum".[32]

Rules 47.09 and 47.10 are frequently discussed and litigated in foreclosure matters. Before the 1995 amendments, Rule 47.09 simply stated that a judgment for any amount due on a mortgage

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[29] This applies only to mortgages entered into or renewed on or after June 30, 1985 (see s.23(1)).

[30] The Nova Scotia Civil Procedure Rules are made by the Judges of the Nova Scotia Court of Appeal and the Supreme Court of Nova Scotia under the authority of the *Judicature Act*, *supra* note 16, ss. 2(h), 46-51 [hereinafter Rules].

[31] Rule 5.13 is also relevant but will not be reviewed here. It provides for foreclosure and sale when the lender has died. Rule 63, dealing with costs, will also not be reviewed here (Tariff B1 sets out solicitor's costs allowable in an uncontested foreclosure proceeding).

[32] Discussed more fully in the following section.

was not to be ordered, entered or enforced before the proceeds of sale were realized. Sale proceeds would therefore have to be deducted from the outstanding balance to determine the actual amount owed. This was changed to provide that "default judgment" would occur "on the earlier of 20 days after the date of sale by public auction or payment to the Sheriff" but judgment for any amount due would "not be entered before the proceeds of sale have been realized and a deficiency, if any, has been determined by the court". It therefore formally required that a deficiency be determined by the court (although Rule 47.10 already provided for an order for deficiency judgment).

The changes also included the addition of subsection 47.09(2). It requires interest on any judgment to be calculated as set out in the *Interest on Judgments Act*.[33] This sets a rate of interest of 5%. This suggests interest is to accrue at 5% from the date of default judgment. Prior practice was to calculate interest at the mortgage rate until the date of the application for deficiency judgment.

Rule 47.10 was also significantly revised in 1995. This Rule relates to deficiency judgments. Rule 47.10(1) allows a lender to get an order for deficiency judgment if the amount realized in a foreclosure sale is insufficient to pay the amount owed. Originally, the Rule indicated a lender "shall" be entitled to an order for payment of the deficiency if it was claimed. The Rule was revised to say a lender "may" be entitled to an order for payment of the deficiency, if it was originally claimed. This change was initially interpreted as giving the court greater direction in fixing a sale price for purposes of calculating a deficiency judgment.[34] Subsequent decisions have, however, cast doubt on this interpretation. The amendment may simply be seen as a recognition of the court's inherent jurisdiction to intervene where appropriate.[35]

Rule 47.10(2) allows the court to deem, or set, the sale price if the lender (or a party related to it) purchases the property at the Sheriff's sale and pays less than fair market value. Originally, Rule 47.10(2) provided that the court, in determining the amount of the deficiency, may deem the sale price to be either the fair market value of the property at the time of the sale (as established by independent appraisal) or the amount realized on a resale of the property if the court is satisfied the price obtained was reasonable. Rule 47.10(2) was revised in 1995 to allow the court to simply deem the sale price to have been the fair market value of the property at the time of the sale. The references to appraisals and resale price were removed.

Rule 47.10(3) provides the time period within which a lender must make an application for deficiency judgment. Originally, the lender was required to make the application within six

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[33] R.S.N.S. 1989, c. 233.

[34] *Toronto-Dominion Bank* v. *Phillips and Ellmore* (1996), 152 N.S.R. (2d) 16 (S.C.).

[35] *Bremner* v. *Royal Bank of Canada* (3 February 1997), Halifax C.A. No. 132524, Nova Scotia Barristers' Society Library No. S407/1 (C.A.) and *Deloitte & Touche Inc.* v. *Spiropoulos*, Decision No. 2, (23 December 1996), Halifax S.H. No. 117301, Nova Scotia Barristers' Society Library No. S408/2 (S.C.).

months from the date of the Sheriff's sale, upon giving 10 days notice. The lender could, however, apply to the court for extensions of time. In 1995 the Rule was amended to require the application be made within six months. It no longer specifically provides for the court to extend the time. In the appropriate circumstances, the court will allow extensions under the discretion granted to courts by the Rules generally.[36] In a recent decision, however, the court denied an application for deficiency judgment made two months after the six month period expired. The court was not satisfied "exceptional circumstances" existed to justify an extension of time.[37]

Practice Memorandum

The Judges of the Nova Scotia Court of Appeal and the Supreme Court of Nova Scotia issue Practice Memoranda on various subjects including foreclosure procedures. Initially issued in 1978, the Practice Memorandum relating to foreclosures was redrafted in March 1994 although there were no substantive changes. Substantial changes were made to Practice Memorandum No. 13, entitled "Foreclosure Procedures", effective September 1, 1995.

Practice Memorandum No. 13 consists of six parts. To date, only two parts have been issued, Part I - General and Part II - Applications for Foreclosure, Sale and Possession. The remaining four parts are "To be issued at a later date" (Part III - Application for Confirmation, Part IV - Application for Deficiency, Part V - Claim against Guarantor and Part VI - Claim of Payment of Surplus).

One of the most significant revisions to Practice Memorandum No. 13 was the addition of a simplified procedure to use in most foreclosure proceedings. Use of the simplified procedure is expected to save time and cost. Forms for use in the simplified procedure are attached to the Practice Memorandum (including Affidavits, the Order for Foreclosure, Sale and Possession and the Notice of Public Auction). The Memorandum indicates the simplified procedure is unlikely to be suitable in applications involving collateral mortgages, complex securities such as debentures, claims under guarantees not contained in the mortgage document and claims for something less than foreclosure, sale and possession. It is expected, however, that the simplified procedure will be appropriate for most foreclosure proceedings.

The revised Practice Memorandum provided a standardized procedure for Sheriff's sales by

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[36] See *e.g., Deloitte & Touche Inc.* v. *Spiropoulos,* Decision No. 1, (23 December 1996), Halifax S.H. No. 117301, Nova Scotia Barristers' Society Library No. S406/12 (S.C.). The court used its general discretion to cure a "minor breach" of the Rules where the lender made the application for deficiency judgment within six months but not with the required ten days notice.

[37] *Inrich Business Development Centre Ltd.* v. *LeBlanc* (9 April 1997), Sydney S.PH No. 01076, Nova Scotia Barristers' Society Library No. 412/28 (S.C.).

public auction. Attached to the memorandum are "Standard Procedure for Sheriff's Sales by Public Auction, Instructions to the Sheriff". Among other things, the instructions set out the circumstances under which the Sheriff is not to proceed to an auction, the amount of the minimum permissible bid, details surrounding the delivery of the Deed to the purchaser and disbursement of the sale proceeds.

Case Law[38]

Much of the law in Nova Scotia regarding foreclosures, particularly deficiency judgments, is "judge made" or common law resulting from court decisions. Cases in this area have focused in two main areas, irregularities in the Sheriff's sale and the duty of the lender to obtain a fair sale price in the context of deficiency judgments.

(i) Irregularities in the Sheriff's sale

The court will scrutinize the conduct and outcome of a sale and where appropriate, set it aside.

In *Bigelow* v. *Blaiklock*[39] several parcels of land, some in Halifax and some outside the City, were sold at a Sheriff's sale. The parcels were advertised in such a way that a purchaser would assume only the parcels outside the City were for sale. They were, however, described differently in the foreclosure documents and mortgage. The lender purchased the properties and the borrower wanted the sale set aside because of the misleading advertising. The court set the sale aside after concluding that the misunderstanding had prejudicially affected the sale. It further found the error was "calculated injuriously to affect the sale by destroying competition" and had resulted in the plaintiff buying the property at a low price.

Another example of an irregularity in the Sheriff's sale is *Confederation Trust Co.* v. *Laconia Gulf Investments Ltd.*.[40] The amount outstanding on the mortgage was over $10 million. The lender's lawyer participated in the bidding in order to achieve as high a price as possible. An individual attending at the sale bid the price up to $6.2 million which the lender's lawyer outbid by $100,000. The individual then ceased bidding leaving the lender as the highest bidder and therefore obliged to pay over $200,000 in property taxes. The lender's lawyer was advised by the individual bidder that while he had been interested in the property, he was annoyed his telephone calls were not returned by the lender and he hoped he had cost the lender a great deal of money. The court concluded the auction was a sham because the bidder was not bidding in

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[38] See MacIntosh, *supra* note 17, for a thorough and detailed review of case law in Nova Scotia dealing with real property generally.

[39] Undated decision but decided between July 1873 and December 1877, Russell's Equity Decisions of Ritchie E.J. 23. See Richardson, *supra* note 9 at 202.

[40] (1993), 123 N.S.R. (2d) 245 (S.C.).

good faith. The ultimate purchaser should not be prejudiced and forced to incur additional and unnecessary expenses as a result. The court therefore set aside the sale and ordered that the Sheriff's sale be rescheduled.

The court refused, however, to set aside the sale in the recent decision of *McInnes Cooper & Robertson et al.* v. *Sea Star Developments Ltd.*[41] The court held the prospective bidders were not misled by the purchaser referring to his bidding partner as another possible bidder. The court did not feel it "dampened" the sale because prospective bidders either did not intend to bid or if they did, they were not misled by the words spoken by the purchaser. As well, the court would not set aside the sale because the purchaser did not provide a certified cheque until 20 minutes after the sale. This constituted payment of a downpayment in a manner authorized by law.

(ii) Duty to obtain fair price in context of deficiency judgments

Courts in Nova Scotia have not hesitated to follow the equitable English practice of looking behind procedure to ensure no unfair advantage is obtained by any party to a transaction. This was first strongly stated in *Central Trust Co.* v. *Adshade*[42] and has been cited by Nova Scotia courts on numerous occasions since then.[43]

In some cases a borrower complains about the price achieved at the Sheriff's sale. For example, in *Briand* v. *Carver*[44] the lender purchased the property at the Sheriff's sale for the minimum permissible bid. The lender used the amount of this bid to calculate a large outstanding deficiency. He then applied to the court for an order for deficiency judgment and to confirm the sale. The court was prepared to confirm the sale only if the deficiency claim was dropped. It found the sale price was so "obviously and grossly inadequate" that it would be inequitable to permit the lender to purchase the property at this price *and* obtain a deficiency judgment for the difference between the purchase price (the bid amount) and the amount owing plus costs.

Although *Briand* v. *Carver* is virtually always cited in subsequent case law on deficiency judgments, its situation is highly unusual. Seldom does the lender purchase the property for the minimum permissible bid and then try to keep it in addition to suing for a deficiency judgment. This is viewed as inappropriate since it results in double recovery and contradicts the idea that a mortgage is only held as security.

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[41] (25 June 1997), Halifax S.H. No. 108767, Nova Scotia Barristers' Society Library No. S413/6 (S.C.).

[42] (1983), 60 N.S.R. (2d) 414 (A.D.).

[43] See *e.g., Montreal Trust Co. of Canada* v. *Moriarty* (1992), 117 N.S.R. (2d) 100 (T.D.) at 106; *Montreal Trust Co. of Canada* v. *Quad-Ram Development Group Ltd. et al* (1994), 136 N.S.R. (2d) 333 (C.A.) at 346; and *Federal Business Development Bank* v. *Silver Spoon Desserts Enterprises Ltd*. (1995), 144 N.S.R. (2d) 161 (C.A.) at 164.

[44] (1967), 4 N.S.R. 1965-69 141 (T.D.).

If a property is sold to a third party at a Sheriff's sale, the courts frequently accept the price obtained at the Sheriff's sale as the best indicator of value. In *Canadian Imperial Bank of Commerce* v. *Simon*[45] a lender bought the property at the Sheriff's sale for $48,000 and resold it for $34,000. A third party had bid $47,500 at the Sheriff's sale. The lender attempted to obtain a deficiency using the resale price of $34,000. The court held the deficiency was to be calculated using the lender's bid of $48,000. The court stated the most reliable evidence before the court as to fair market value was "what was bid at the sale where two willing buyers bid against each other".[46]

This was recently confirmed by the Nova Scotia Court of Appeal in *Canadian Imperial Bank of Commerce* v. *England's (R.) Warehouse Ltd.*[47] The court held the price bid by an independent third party at the Sheriff's sale must be used in calculating the deficiency judgment "...in the absence of some conduct of the mortgagee [lender] in relation to the Sheriff's Sale that would compel the court to exercise its equitable jurisdiction and reach another conclusion".[48] The court acknowledged, however, the inadequacy of the Sheriff's sale in achieving fair market value:

> *"Fair market value will not necessarily be achieved at a Sheriff's sale. Such a sale, although by way of public auction, is, in a sense, a forced sale and is, therefore, different than a sale on the open market. A potential purchaser is unlikely to have an opportunity to inspect the interior of the property as usually the mortgagor is still in possession and is not anxious to co-operate. This, of course, has a dampening affect on the price that can be obtained at a Sheriff's sale; the bidder is, to a certain extent, buying a "pig in a poke" so to speak. Even though the Sheriff is a willing seller he does not have as his goal obtaining a fair market value. His duty is to conduct the sale in a judicial manner in accordance with the directions in the foreclosure order and the established practice. Experience has shown that properties are often sold at Sheriff's sales to the mortgagee for a nominal sum which is well below anything that is either reasonable or representative of fair market value. ... The reality is that Sheriff's sales at public auction, despite the advertising and the notices to subsequent encumbrances, are often not very much like sales between willing*

[45] (1992), 111 N.S.R. (2d) 404 (T.D.).

[46] *Ibid.* at 407.

[47] (1996), 147 N.S.R. (2d) 321 (C.A.).

[48] *Ibid.* at 341.

sellers and willing buyers on the open market."[49]

Much of the case law deals with situations where a lender purchases the property at the Sheriff's sale and resells it. If the resale price does not cover the amount of the mortgage debt plus expenses, the lender may apply for a deficiency judgment calculated using the resale price. The borrower may challenge the resale price as not being adequate.

In *Royal Trust Corp. of Canada* v. *Offman*,[50] the lender purchased the property for under $50,000. The property was resold for $260,000. The three appraised values ranged from $285,000 to $886,000. The appraised value prior to granting the mortgage two years earlier was $1,600,000. The trial judge granted the lender a deficiency judgment using a "deemed sale price" of $500,000. The Court of Appeal, however, concluded the trial judge erred in failing to use the resale price as indicative of the fair market value. The court stated that resale price should be used if the court is satisfied the resale price is reasonable:

> *"In this event, the market has determined the fair market value and the opinions of the experts, which are invariably based on estimates and assumptions about future events, although useful, are not determinative. If the property has been exposed to the market for a significant period of time, a number of offers received, the purchaser is at arm's length from the vendor, and vigorous marketing efforts have been undertaken, the court should not be hesitant to find that the price obtained was reasonable, unless there is some persuasive evidence to the contrary."*[51]

A similar result was found in *Confederation Trust Co.* v. *Wheel House Investments Ltd.*[52]. The court noted the property was listed on the open market for a considerable period of time (one year). The court was satisfied this was evidence of fair market value on which the court was entitled to rely.

Courts may also rely on appraised values as fair market value when calculating deficiency judgments. This can occur when the court rejects the resale price as not being reasonable. It can also occur if the lender has been unable to sell the property and is forced to make an application for a deficiency judgment before the time for doing so expires.

The court rejected the resale price as not being reasonable in *Federal Business Development*

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[49] *Ibid.* at 335-6.

[50] (1994), 132 N.S.R. (2d) 306 (C.A.).

[51] *Ibid.* at 309-10.

[52] (1994), 136 N.S.R. (2d) 147 (C.A.)

Bank v. *Silver Spoon Desserts Enterprises Ltd.*[53] The lender purchased the property at the Sheriff's sale and sold it to a third party for $325,000. The trial judge used the "forced sale" appraisal value of $370,000 as representing fair market value. He was not satisfied the resale price was "reasonable" because the property was sold quickly and without adequate publicity. The Court of Appeal adjusted the "forced sale" price to arrive at a figure of $480,000. It felt certain adjustments were required to the appraisal amount as expenses were included that should not be charged to the borrower.[54]

In *Montreal Trust Co. of Canada* v. *Grab and Kohl*[55] the lender applied for a deficiency judgment using appraised values as the deemed sale price because the three properties had not yet been resold. There were three appraisals on each property with the lowest appraisal being half the value of the highest ($600,000 versus $1,200,000.). The two lower appraisals were submitted by the lender, the highest was submitted by the borrower. The trial judge heard evidence from the three appraisers and analyzed the differences between the methodologies. She accepted the middle appraisal as appropriate. The Court of Appeal did not interfere with her finding.

Toronto-Dominion Bank v. *Phillips and Ellmore*[56] is one of the first cases to consider the new Rules, as amended in 1995. Prior to the amendments, the court was restricted, under Rule 47.10(2), to deeming the sale price to be either the fair market value as established by appraisal or the amount realized on resale if the court was satisfied the amount was reasonable. The amendments simply indicate the court may deem the sale price to have been the fair market value at the time of the Sheriff's sale. The court concluded that previously decided cases interpreting Rule 47.10(2) no longer applied. The court further stated:

> *"Greater discretion has now been given to the court to fix the sale price for purposes of determining the deficiency*".[57]

While the court accepted the resale value as the sale price to be used in calculating the deficiency, it denied the application for deficiency judgment due to apparent non-compliance

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[53] (1995), 144 N.S.R. (2d) 161 (C.A.).

[54] See *e.g., Scotia Mortgage Corp.* v. *Close* (1992), 114 N.S.R. (2d) 65 (T.D.) and *CIBC Mortgage Corp.* v. *Levert et al* (1994), 135 N.S.R. (2d) 1 (S.C.).

[55] (1995), 139 N.S.R. (2d) 343 (C.A.).

[56] (1996), 152 N.S.R. (2d) 16 (S.C.).

[57] *Ibid*. at 17.

with the revised Rules.[58] The interest rate was not as set out in the *Interest on Judgments Act*[59]. As well, the plaintiff claimed expenses beyond 20 days after the Sheriff's sale. The Court of Appeal, however, further clarified the meaning of the changes in *Bremner* v. *Royal Bank of Canada*.[60] It said the amendment was simply a recognition of the court's inherent jurisdiction to intervene in the appropriate case. It did not place additional obligations on the lender other than those already provided in the Rules.

3. The law in other Canadian jurisdictions[61]

In Canada, there are essentially two ways a lender can realize on security when the borrower defaults: "judicial sale" or "power of sale". A judicial sale is a sale made under an order of the court or one which is conducted under the supervision of the court. A judicial sale is sometimes referred to as "foreclosure and sale" because it has the same effect in that the borrower's right to redeem is extinguished if the debt is not paid within the time set by the court.[62]

Six provinces have adopted judicial sale as either the primary or sole vehicle for recovering the mortgage debt: British Columbia, Alberta, Saskatchewan, Manitoba, Quebec and Nova Scotia. The Nova Scotia system is known as judicial sale because it is conducted under court order and is supervised by the court. Judicial sale is also available in Ontario but is rarely used because lenders prefer to use the power of sale contained in the mortgage agreement.

While these provinces each use the judicial sale system, the practice in each province varies widely. In Alberta and Manitoba, for example, a foreclosure order can only be requested once it is shown the mortgaged property was offered for sale at public auction, that appropriate notice was given and the highest bid was insufficient to extinguish the mortgage debt.

Only Ontario and British Columbia have developed procedures which attempt to expose the property to the market and obtain as high a price as possible. In British Columbia, the court has a wide discretion to order a sale in any manner it feels appropriate. Orders frequently permit listing of property with a real estate agent under exclusive or multiple listing agreements. The purchase price and terms of sale must be approved by the court. The court also determines the amount of commission to which the real estate agent is entitled. As well, the order usually instructs the lender to show the property to perspective purchasers between specified hours.

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[58] This decision was recently cited with approval, *supra* note 37.

[59] *Supra* note 33.

[60] *Supra* note 35.

[61] Most of the information contained in this section has been taken from J.E. Roach, *The Canadian Law of Mortgages of Land* (Toronto: Butterworths, 1993) and J.T. Robertson, "The Problem of Price Adequacy in Foreclosure Sales" (1987) 66 Can. Bar Rev. 671.

[62] Roach, *ibid.,* at 107.

Posting of "for sale" signs is also permitted. Another aspect of British Columbia practice is unique: if there is more than one lender, the party having conduct of the sale is generally the one with the least priority. This lender is motivated to ensure the highest possible purchase price is obtained to ensure there will be sufficient proceeds to pay this lender, after the other lenders are paid. Overall, the British Columbia practice is seen as most concerned with protecting borrowers:

> *"When compared to a judicial sale as pursued in the other provinces, it would unwarranted to criticize British Columbia practice for it is quite evident that the foreclosure process is primarily concerned with protection of debtors when dealing with sale procedures and sale price."*[63]

The second way a lender in Canada can realize on security is "power of sale". This refers to the situation where the lender pursues a sale privately or through public auction but without the involvement of the court. It is the main remedy used in New Brunswick, Prince Edward Island, Newfoundland and Ontario. In fact, in New Brunswick, it is the *only* method used as judicial sale does not exist. Power of sale is preferred in Ontario and Prince Edward Island because of dissatisfaction with the judicial sale process. In Newfoundland, it is preferred because it is easier to implement.

The process used in New Brunswick, Prince Edward Island and Newfoundland has still been criticized as not ensuring adequate exposure to the market in order to obtain the highest possible resale price. Neither province sets out the marketing process to be followed but leaves it to the lender to decide whether the sale is to be sold by public auction or private contract. Advertising is often limited and seen as inadequate.[64] In Ontario, on the other hand, accepted practice is to list the property for sale with a real estate broker. It is believed that Ontario, of the four provinces using power of sale, is the only one adequately addressing the need to develop marketing practices aimed at achieving the highest possible resale price.[65]

4. Empirical study of foreclosure files

In order to more fully understand how the foreclosure process is working in Nova Scotia[66], a study was conducted of all foreclosure files opened in the Halifax County Sheriff's Office over a 2 ½ year period (January 1, 1994 to June 30, 1996). A total of 383 files were examined. Of the

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[63] Robertson, *supra* note 61 at 681.

[64] *Ibid.* at 682.

[65] *Ibid.* at 707.

[66] According to statistics kept by the provincial Department of Justice, foreclosure sales in Halifax County constitute between 1/3 and ½ of all foreclosure sales in Nova Scotia.

383 files, 52 were discontinued and therefore did not result in sales conducted by the Sheriff's Office.[67] The remaining 331 files were the subject of this study.

Information gathered in the study included: the time it took to have a foreclosure sale once the lender sued the borrower, whether the property was purchased at the Sheriff's sale by the lender or a third party; whether the sale price was adequate to cover the mortgage debt and whether surpluses existed; the amount outstanding on the mortgage account; and the frequency and amount of deficiency judgments.

How long does it take to hold a Sheriff's sale?

In the files studied, the time between the court order and the Sheriff's sale varied from 10 days to 539 days, for an average of six weeks. The majority of sales, took place between 30 and 50 days after the court order.

What is the amount of the outstanding mortgage debt?

In 20% of the files studied, the debt at the date of the court order was less than $50,000. Forty percent of the files showed debt between $50,000 and $100,000. Twenty percent were between $100,000 and $250,000 and 20% were over $250,000.

Who purchases at the Sheriff's sale?

In 16% of Sheriff's sales in the study, the property was purchased by a third party unrelated to the lender. In the remaining 84% of sales, the property was purchased by the lender. The lender has the option of taking title in its own name or, within 20 days of the sale, requesting that the Sheriff's Deed be made out to a third party (this eliminates the need for the lender to pay Deed Transfer Tax). In 9% of the sales to lenders, the lender requested an assignment to a third party before the end of the 20 day period. Assuming the third party is not related to the lender, this means 23% of all Sheriff's sales result in the property being sold to a third party at the time of or within 20 days of the Sheriff's sale. In the remaining 77% of sales, the property was conveyed to the lender. Presumably, the lender would then attempt to sell the property on the open market.

Did the purchase price cover the amount owed?

Only 10% of all Sheriff's sales resulted in a surplus to the credit of the borrower once the mortgage debt and all associated costs were paid. Almost 60% of sales to unrelated third parties resulted in a surplus. Only 1.4% of the sales to lenders resulted in a surplus.

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[67] Lenders agree to discontinue foreclosure proceedings for numerous reasons including agreements to refinance, the borrower making payments and the lender agreeing to reinstate the mortgage, the borrower finding a purchaser (acceptable to the lender) prior to the Sheriff's sale, or the lender agreeing to take the property in satisfaction of the debt.

Of sales to unrelated third parties, almost 90% were for a purchase price above, or no more than 15% below, the amount outstanding on the mortgage. In almost 75% of sales to lenders, the lender purchased for what is know as the "minimum permissible bid" (the sum of the Sheriff's fees and outstanding property taxes).[68] Although no record is kept of attendance, in most of these cases it is assumed the lender was the only bidder at the Sheriff's sale.

Deficiency Judgments

Once a Sheriff's sale is held, the lender has six months to apply for a deficiency judgment. As a result, this part of the study was based on Sheriff's sales over the first two years of the 2½ year survey period (January 1, 1994 to December 31, 1995). During this period, 265 Sheriff's sales were held. There was a surplus in 13% of the sales, leaving 87% of sales in which the lender could apply for a deficiency judgment.

Of the 87% of cases with a deficiency, a deficiency judgment was applied for in just over one-quarter of the cases. One can speculate as to the reasons why a deficiency judgment was not sought in almost 75% of the cases where a deficiency exists. In some cases, the deficiency amount may be so low that the costs of an application are not warranted. In other cases, the chances of collecting on a judgment may be minimal.[69]

When a deficiency judgment is requested, the application if successful 85% of the time. Three-quarters of the deficiency judgments obtained are for amounts less than $50,000. In over half of the successful applications, the deficiency was calculated using the purchase price from the Sheriff's sale or, more commonly, the purchase price on a resale to a third party. The remainder of the successful applications used appraisal evidence to establish a "purchase price" to be used in calculating the deficiency.

Conclusions from Empirical Study

From the results of the study, it is clear the current system is not meeting its objectives. Sheriff's sales no longer attract third party bidders. Competitive sale prices are rarely obtained with 90% of sales resulting in a deficiency. Of the 10% of sales resulting in a surplus, the large majority result from sales to third parties.

In 77% of Sheriff's sales, lenders ended up owning the properties. Presumably, they attempt to resell the properties on the open market. Costs incurred in this process are to the borrower's account and can be added to the amount claimed in any application for deficiency judgment.

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[68] Practice Memorandum No. 13, "Standard Procedure for Sheriff's sales by Public Auction, Instructions to the Sheriff", s. 2(a) at 34.2. The *Assessment Act*, R.S.N.S. 1989, c. 23, s.122 requires the Sheriff to pay outstanding taxes from the sale proceeds.

[69] If the borrower is a corporation, it may have no assets. If the borrower is an individual, he or she may have no assets and may consider declaring bankruptcy should a judgment be obtained.

Lenders rarely apply for a deficiency even though a deficiency exists in almost 90% of cases. While lenders have the option of applying for a deficiency judgment after the Sheriff's sale, if they buy the property at the Sheriff's sale and later resell it for more than the amount owed, they are not required to remit any surplus to the borrower[70].

The results of the empirical study suggest the system is no longer meeting the needs of borrowers or lenders. The following section explores the need for reform. The fairness of the system is then reviewed followed by specific suggestions for improvement.

[70] Civil Procedure Rule 47.11 requires the lender to distribute any surplus when "the purchase money on a sale exceeds what is found to be due". It is understood the word "sale" refers to the Sheriff's sale and not a resale *after* the lender purchases the property at the Sheriff's sale.

III SUGGESTIONS FOR REFORM

1. Is reform necessary?

The current system is problematic for both borrowers and lenders. From a borrower's point of view, there are several problems. For one, the process is totally within the lender's control. Borrowers rarely retain a lawyer to represent them and virtually all applications for foreclosure and sale are undefended. For the most part, the process unfolds without the borrower's participation and in the absence of any information about their rights or about the foreclosure process itself.

The borrower continues to be responsible for interest and costs which accumulate after the lender starts the foreclosure process. Costs may be substantial if the property is on the market for a period of time but does not sell. Anecdotal evidence suggests there have been cases where a shortfall has doubled between the time the initial order is granted and the time the lender applies for a deficiency judgment.

Overall, the foreclosure process is not oriented toward achieving the best possible price for the property. Property is sold by the Sheriff through public auction. In the 19th Century this method was considered most effective to encourage competitive bidding and achieve the highest possible purchase price. At that time, advertising in public papers and posting handbills on town walls were viewed as effective marketing techniques.[71] Foreclosure by public auction conducted by the Sheriff is no longer achieving the objectives of providing competitive bidding and fair prices while also preserving a lender's right to apply for any deficiency.[72] As the Commission's study of foreclosure files revealed, an unrelated third party purchased the property in only 16% of the cases. The lender purchased in the remaining 84%. Presumably, no other bidders attended at the sales at which the lender purchased the property. Overall, a surplus existed in only 10% of all the files studied. The fact that a deficiency exists in almost 90% of the files studied shows the current system is simply not working for either the borrower or lender. The foreclosure process should more closely resemble a sale on the open market. It should generate sufficient interest to encourage competitive bidding and a purchase price at or near fair market value.

In 84% of the foreclosure files studied by the Commission, the lender purchased the property for a nominal sum (Sheriff's fees and outstanding property taxes). The lender then attempts to sell the property on the open market. If the resale price is inadequate to pay the mortgage debt and associated costs, the lender has the right to apply for a deficiency judgment. If, however, the resale price is greater than the mortgage debt and associated costs, the lender does not have a duty to account to the borrower for any profit. It is not known whether or how often this occurs. In the current economic conditions, it is not likely a common occurrence.

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[71] Robertson, *supra* note 61 at 684.

[72] *Supra* note 14 at 884.

The Sheriff's sale is also an expensive step which may not be required if a private sale to a third party could be arranged by the parties after the Order for Foreclosure, Sale and Possession is issued. Expenses incurred in the Sheriff's sale include the Sheriff's fees, costs for placing two advertisements in the newspaper, and solicitor's fees in preparing the documents and in arranging and attending at the sale. Given that the Sheriff's sale is largely ineffective in providing competitive bidding and fair market prices, the expense may not be justified. If the parties are able to arrange a private sale to a third party, they should not be prohibited from doing so.

The present system presents the appearance of a conflict of interest by allowing the lender to bid at the Sheriff's sale. This practice is forbidden in most jurisdictions. It is believed most lenders do not wish to own properties and would prefer to satisfy the mortgage debt, as far as is possible, conclude the matter and avoid further expense.

Problems also exist from the lender's point of view. Delays in realizing on the security are problematic. The process is unnecessarily time consuming and cumbersome. Lenders continue to incur legal fees throughout the process. The Commission's study of foreclosure files showed the time period between the initial Order and the Sheriff's sale varied from a low of 10 days to a high of 539 days, for an average of six weeks. The majority of sales took place between 30 and 50 days after the Order. Given that the lender purchased the property in 84% of the sales, it is clear the process does not end there. Although the data is not available, it is assumed in many cases a resale of the property to a third party would take some time, particularly given current economic conditions. The lender would continue to incur expenses including management and maintenance costs. Admittedly, it could attempt to recover these costs on an application for deficiency judgment. Chances of recovery may, however, be minimal.

In some cases, lenders forego seeking deficiency judgments to which they may be legitimately entitled, even when the borrower is not bankrupt and there may be some chances of collecting on the judgment. As the Commission's study of foreclosure files showed, a deficiency judgment is requested in less than 30% of the cases where a deficiency exists. Should an application for a deficiency judgment be successful, the lender then incurs collection costs which can include legal fees, Sheriff's fees, Bailiff's fees and the cost of registering judgments.

It is believed lenders do not wish to become owners of the foreclosed properties. Most lenders are not in the business of property ownership and management. They would prefer to realize on their security and conclude the process as quickly as possible. Lenders also face other disincentives to ownership such as environmental liability and the requirement that the lender incur the cost of any clean up. The costs of such clean up may not be allowed on an application for deficiency judgment.

In addition to losing some or all of the funds advanced under the mortgage, lenders often incur further expenses once they foreclose and take possession of the property. These expenses may not be recovered on an application for a deficiency judgment. These expenses include costs of property management, costs of appraisals, cost of environmental assessments and clean up, and

so on. This further increases the funds owed to the borrower, some or all of which may not be collected.

Changes were made to the Rules and Practice Memorandum on September 1, 1995. It is believed these changes were intended to provide more protection to the borrower. For example, the courts initially interpreted the amended Rules to mean no expenses relating to maintenance of the property would be allowed beyond 20 days after the Sheriff's sale. The impact of the changes remains to be seen.

The Commission suggests:

The law relating to mortgage foreclosure and sale in Nova Scotia be reformed.

2. Is the current system fair?

The principal goal of the current system is to protect the lender's security interest by ensuring the property is sold and the money recovered for the benefit of both the lender and the borrower. A secondary goal is to protect the borrower's interest, particularly in any equity built up, and in the context of any deficiency owing once the property is sold. These diverse interests must be balanced. Borrowers must have reasonable access to credit in order to enable them to purchase property. Lenders must be able to profitably provide such credit while having access to remedies should the borrower default.

It is clear the Sheriff's sale is no longer the appropriate measure for achieving fair market value for a property. In the Sheriff's sales studied by the Commission, an unrelated third party purchased the property in only 15% of the cases. It was only in this small percentage of cases that a purchase price approaching market value was achieved. In fact, a surplus on the mortgage account existed in 60% of the sales to third parties and in only 1% of the sales to the lender. Overall, a surplus existed in only 10% of all the Sheriff's sales studied. A deficiency existed in 90% of the sales. Clearly the Sheriff's sale is no longer an appropriate mechanism for the lender to realize on security and achieve the best possible resale price. This was recently recognized by the Nova Scotia Court of Appeal[73] where it was observed the Sheriff's sale often has a "dampening effect" on price because a potential purchaser is unlikely to have an opportunity to inspect the property and because the Sheriff's goal is not to obtain a price reflecting fair market value.

Nova Scotia law fails to impose many demands on a lender who resells property after purchasing it for a nominal price at a Sheriff's sale. While a lender owes a duty of care to realize a "reasonable price" on a resale, the standard of care to justify that duty is less onerous than in

[73] *Supra* note 47.

some other jurisdictions. There is, for example, no duty to advertise or list the property with a real estate agent. The court will be reluctant to reject the price achieved at a resale as the basis for calculating the amount of a deficiency unless the borrower can show a gross disparity between that price and any appraisal evidence, or can point to some obviously improper act in the course of the sale.[74]

Currently, if the lender resells the property at a profit after purchasing it at the Sheriff's sale, there is no duty to account to the borrower for the surplus. If, however, the property is sold for less than the amount of the mortgage debt, it can sue the borrower for the deficiency.

While it recognizes lenders often lose money in foreclosure cases, the Commission believes the foreclosure system in Nova Scotia is unfairly balanced in favour of lenders and does not adequately protect borrowers.

The Commission suggests:

The current system of foreclosure and sale is unfairly balanced in favour of lenders and does not adequately protect borrowers.

3. Should the Sheriff's sale be reformed or abolished? If abolished, how should it be replaced?

Sale of land at public auction has long ceased to be an effective means of realizing market value. The Commission believes it is widely recognized the Sheriff's sale is a total anachronism in today's environment.

The Commission considered three types of reform: (i) private sale after obtaining the initial court order; (ii) private power of sale; and (iii) modified judicial sale.

(i) Private Sale after Initial Court Order Obtained

Under the first option, the lender would be authorized to sell the property by private sale, after obtaining an Order for Foreclosure, Sale and Possession, but before the Sheriff's sale was conducted. The sale would require court approval. The court would grant approval if the court is satisfied: (a) the purchase price is at least is great as the sum outstanding on the mortgage, or the lender has agreed to accept the purchase price in full satisfaction of the

[74] *Ibid*.

mortgage debt; and (b) the purchase price represents fair market value of the property, or if the borrower (and all other interested parties) have consented to the sale.

While this procedure provides an alternative to the Sheriff's sale, it remains entirely within the control of the lender. It is unclear whether there would be sufficient incentive for the lender to seek out a third party purchaser. If the lender knew the property would be relatively easy to sell, it would make more sense to acquire title at the Sheriff's sale, resell the property and keep any surplus. If the right to retain a surplus were abolished, the lender would presumably wish to dispose of the property as quickly as possible and avoid incurring further expense.

The Commission concluded this version of reform would not be adequate. It would leave the lender in control of the process and not result in significant change from the current system.

(ii) Private Power of Sale

A more fundamental type of reform is private power of sale. This would involve abolishing the judicial sale (including the Sheriff's sale) and replacing it with a private "power of sale".[75] Ontario, Newfoundland, New Brunswick and Prince Edward Island authorize lenders to carry out the sale themselves. In Ontario, for example, 15 days after default occurs, notice of intent to exercise the power of sale is given to the borrower and to all other persons having an interest in the property. The power of sale cannot be exercised until 35 to 45 days after the initial notice is given. The parties may, however, stipulate for longer periods. At present there is no statutory regulation of the manner in which the sale must be conducted although case law has tended to restrict such sales rather stringently. Private powers of sale are not, however, totally outside judicial scrutiny. A borrower may seek to set a sale aside on the basis that it was conducted improperly. If a lender seeks a deficiency judgment, it obviously will still have to apply to the court. At that time, the borrower may argue that the sale was conducted improperly and the amount of any deficiency should therefore be reduced. The court is also involved in that the exercise of the power of sale is normally preceded by an application for possession and for judgment on the mortgage covenant.

A principal advantage of private power of sale is that it would be clearer to borrowers than the current foreclosure process. It turns foreclosure into a more straightforward accounting process and allows the borrower to see the money produced from a sale and where it is gone. There is no possibility of the lender keeping a surplus should one be generated but an application for a deficiency judgment can be brought if the sale price does not cover the mortgage debt. The power of sale approach in Ontario imposes fairly strict guidelines on the lender's conduct of the sale. Another advantage of power of sale is reduced demands on court time and reduced court

[75] See Part II.3., above.

costs. Legal fees are also lower especially if the lender does not seek a judgment against the borrower and the borrower vacates the property when requested. Private power of sale may also be seen as more convenient for lenders because of less supervision by the court.

There are several concerns with the private power of sale. One is how to adequately protect the interests of the borrower in a non-judicial proceeding. In addition, increased costs accrue to the borrower's account while the property is being marketed for sale. Another concern is how to respond when the property does not sell. A lender is not permitted to purchase the property when the private power of sale is used. The Ontario *Mortgages Act*[76] contains ways to deal with this issue. One is through a sale at public auction but the more usual recourse is to terminate the notice of sale process and revert to a straight foreclosure process through the court (this gives the lender full title to the property in satisfaction of the debt). This would have to be addressed in Nova Scotia as it is perceived the real estate market is not as active as in certain areas of Ontario. Another disadvantage of private power of sale is that it does not necessarily result in a speedier sale of the property because a sale is dependent on market conditions. Finally, a power of sale is no guarantee that an adequate sale price will be achieved.

(iii) Modified Judicial Sale

The Commission recommends a "modified judicial sale". It suggests that the Sheriff's sale be abolished and replaced with a different type of judicial sale.[77] In suggesting this type of reform, the Commission recognizes a number of objectives in reforming foreclosure and sale in Nova Scotia:

- There is a desire to keep the court involved to oversee the process although less use of court time is also desired.

- The proposed system must attain a better price for the property than currently achieved under the Sheriff's sale. Ideally, the price would be greater than, or as close as possible to, fair market value.

- There is a wish to avoid, as much as possible, the borrower losing the property *and* facing a large deficiency judgment.

- Costs must be minimized, as much as possible, after the lender takes possession of the property.

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[76] R.S.O. 1990, c. M. 40.

[77] As outlined in Part II.3., above, a judicial sale is a sale made under an order of the court or one which is conducted under the supervision of the court. The Sheriff's sale in Nova Scotia is therefore part of a judicial sale system. The Commission is recommending the system still be overseen by the court but that the sale be conducted in a different manner.

- The proposed system must be balanced and must continue to enable lenders to provide credit to borrowers at a reasonable rate.

The Commission is proposing a modified judicial sale based on an equity/no equity distinction. A property is considered to have equity when the appraised value is greater than the amount owed. A surplus will therefore exist at the time the Order for Foreclosure, Sale and Possession is granted. If the appraised value is less than the amount owed, the property is considered to have no equity and there is already a deficiency at the beginning of the process.

The equity/no equity distinction relies heavily on the use of appraisals. Many court decisions note inconsistencies in appraisals and disparities in valuation. In some reported decisions, lenders provide appraisals which indicate the property value to be low while borrowers provide appraisals which indicate the property value to be high. The modified judicial sale process would have to include adequate safeguards to overcome any deficiencies inherent in relying upon appraisals. For example, it would have to require that the lender automatically provide the borrower with a copy of the appraisal done at the time of the mortgage. The appraisal prepared for the lender at the time of default would have to be attached to the notice of the application of the Order for Foreclosure, Sale and Possession. The appraisal would have to be independent in that it could not be done by a company owned by or related to the lender. It would have to explain *any* discrepancy from the appraisal done at the time of the mortgage. The appraisal would be paid for by the lender who would only be required to obtain one appraisal at the time of default. Since the appraisal would be attached to the notice of application, all parties (including subsequent encumbrancers) would have an opportunity to review and challenge it. Challenges would be based not only on appraisals prepared for other parties but on actual offers to purchase the property. This would reflect the comment frequently made by the court that the best indicator of fair market value is the price a willing seller expects to receive from a willing buyer on the open market.

The Commission's suggestions for a modified judicial sale are outlined more specifically below. The process to be followed for when there is equity in the property is outlined first, followed by a description of the process to be followed when there is no equity in the property.

Equity in the Property - Surplus to start with

A property is said to have equity if the appraised value is greater than the amount owed on the mortgage. If, for example, the amount owed at the time of foreclosure is $100,000 and the appraised value is $120,000, a surplus of $20,000 is considered to exist. In these circumstances, it is in both the lender's and borrower's best interests to attempt to obtain a resale price as close as possible to the appraised value. The property would be listed on the open market with a real estate agent for a fixed period of time, such as four months. It could be listed with the lender's real estate company if the lender wished. Renewals of the initial four month listing period could be agreed to by all parties.

Once the property is listed on the market, a sale could occur at various possible purchase prices. If the purchase price is greater than the appraised value, the lender would account to the borrower, and other encumbrancers (in order of priority), for the surplus. If the purchase price is less than the appraised value but more than the amount owed, the lender would have no choice but to agree to a sale because the lender's debt would be fully covered by the purchase price. However, the borrower and other encumbrancers would have to consent to the sale because their claims would likely be compromised as a result of the reduced sale price. If the purchase price was less than the amount owing, the sale could only proceed if the borrower agrees and if the lender and other encumbrancers agree to accept this amount in full satisfaction of the debt.

If no sale is achieved, the lender would have two options. The *first option* would be to accept the property in full satisfaction of the debt. This would be similar to a true foreclosure in that the security satisfies the debt and there is no sale as part of the process. There would be no surplus to the borrower even though the appraised value of the property is more than the amount owed. This could create a possible inequity if, for example, the lender kept the property on the market and eventually resold it for an amount greater than the amount owed. Using the example outlined above, the lender may sell the property for $110,000 six months after the initial listing period expired. The lender therefore has a surplus of $10,000 over the $100,000 owed. Assuming this surplus has not been consumed by resale, property management and other costs, the lender might be expected to account to the borrower for the surplus. Logistically, it would be extremely cumbersome and difficult to follow the lender indefinitely. In some cases, the property may not sell for one or two years. It would be inappropriate to require the lender to continue to report to the court for this period of time. Similarly, should the lender ultimately resell the property for less than the amount owed, it would not be permitted to apply for a deficiency judgment against the borrower. For example, if the debt was $100,000 and the property ultimately sold for $80,000, the lender would not be permitted to seek the $20,000 shortfall from the borrower. In any event, the Commission suggests that the risk of the lender gaining a surplus can be counteracted by the borrower having the right to vigorously market and attempt to sell the property during the initial four month listing period.

If there is no sale, the *second option* available to the lender would be to surrender the property to subsequent encumbrancers in order of priority. In the standard residential foreclosure, however, there are often no encumbrancers other than the lender. If each encumbrancer refuses to take the property in satisfaction of their debt, the property would be returned to the borrower. All encumbrances would be released as they refused to take the property. The lender's recourse would then be to sue on the covenants in the mortgage for the full amount owing. This is a right that has always existed because a mortgage usually consists of two parts: (i) the property as security for the debt and (ii) the covenant, known as the "personal covenant", by which the borrower agrees to repay the debt independent of the property. The personal covenant enables the lender to refuse to take the property and instead sue for the full amount owing under the covenants in the mortgage.

No Equity in the Property - Deficiency to start with

The second possible scenario under the modified judicial sale process is that there is no equity in the property at the time the order is granted. This would occur, for example, if the amount owed was $100,000 and the appraised value was $80,000. There would therefore be a $20,000 deficiency to start with. The issue is how to pay as much of the debt as possible, while not adding to the deficiency by incurring further costs which will ultimately have to be paid by the borrower. Since a shortfall already exists, there is a concern that it not be further increased while the lender attempts to resell the property. Anecdotal evidence suggests there have been cases where a shortfall has doubled between the time the order is granted and the time the lender applies for a deficiency judgment.

In order to achieve the objectives of enabling the lender to recover as much of its debt as possible, while not increasing the amount of the deficiency which already exists, the Commission suggests giving the lender two options. The *first option* would be to accept the property in satisfaction of the debt with a right to apply for a deficiency judgment against the borrower. The lender would accept the property based on the appraised value and be required to apply for any deficiency immediately, thereby preventing further costs accruing to the account of the borrower. In the example used above, the lender would acquire the property at a deemed value of $80,000 and would apply for a deficiency judgment in the amount of $20,000. The *second option* open to the lender would be similar to that outlined above when there is equity in the property and no sale has occurred. That is, the lender would surrender the property to other encumbrancers in order of priority. Upon each encumbrancer refusing to take the property, the encumbrance would be released. Ultimately, if all encumbrancers refused the property, it would go to the borrower. The lender could then sue the borrower, under the covenants in the mortgage, for the full amount owing.

The Commission suggests:

- Sheriff's sales be abolished and replaced with a sale on the open market, depending on whether there is equity in the property at the time of foreclosure.
- If there is equity in the property, it would be listed with a real estate agent. If the property did not sell, the lender could either accept the property in full satisfaction of the debt or surrender the property to subsequent encumbrancers (in order of priority) and sue the borrower for the full amount owing.
- If there is no equity in the property, a foreclosure order could be issued immediately and the lender could apply for a deficiency judgement based on the appraised value. If the lender did not wish to accept the property, it could surrender it to subsequent encumbrancers (in order of priority) and sue the borrower for the full amount owing.

It has been suggested that the Commission consider the approach used in other provinces,

such as Ontario, which allow the borrower to list the property for sale. In Ontario this usually occurs once the borrower goes into default. The borrower recognizes it would be in its best interests to attempt to sell the property as quickly as possible. The lender then sends out the notice of power of sale, and the borrower continues to list the property during the 35 to 45 day notice period. At the end of this period, the lender must decide whether the borrower is adequately marketing the property and whether it is listed at a reasonable price. If the lender is satisfied with the borrower's efforts, the lender may do nothing. This generally works well because the borrower is highly motivated to market and sell the property. A problem arises if the lender is not satisfied with the borrower's efforts and wishes to also list the property. This results in a dual listing. The lender cannot prevent the borrower from continuing to list the property as it has the right to do so during the redemption period (in Ontario, the redemption period exists until the lender enters into a binding agreement of purchase and sale with a third party buyer). The Commission invites comments on the concept of dual listing.

The Commission also invites comment on the issue of chattels in foreclosed property. If chattels are used in connection with the property, the question arises as to whether they should be realized with the property.

4. Is there a need to make the process clearer to borrowers?

The Commission believes there is a need to make the foreclosure process clearer to borrowers. Virtually all foreclosure actions are undefended and in most cases there is no valid legal defence. Borrowers in default are unlikely to seek legal advice because they assume they have no options and because, by virtue of their financial predicament, they are unable to pay for a lawyer. As well, the level of experience of borrowers varies significantly. Some will have no familiarity with using lawyers and may be uncomfortable with the process generally.

Since it appears there is a need to make the process clearer to borrowers, the issue then becomes when to provide the information. It could be provided before or at the time of signing the mortgage. One option considered by the Commission was requiring lenders to provide borrowers with a pamphlet outlining their rights upon default. Such a pamphlet could emphasize that borrowers may lose equity in their home and owe more money after foreclosure, in the form of a deficiency judgment. It is believed, however, a separate pamphlet is not workable. The mortgage document would contain much more information than the pamphlet and litigation may arise if a borrower claims to have relied on the pamphlet for legal advice. As well, there are a number of concerns with providing information on default at this time:

- Such a large volume of information is provided at this time that information relating to default will not likely be recalled or appreciated. This will be especially true for inexperienced borrowers.
- The time period between signing the mortgage document and going into default may be significant. The information provided at the time of signing the mortgage will often be forgotten.
- From a practical perspective, it would be virtually impossible for a lawyer to explain all

parts of a technical, legal document, such as a mortgage agreement, without making the process extremely costly.

- Even after having been advised of the process once default occurs, the majority of borrowers will still sign the mortgage document.

The Sheriff's Office, the Public Legal Education Society of Nova Scotia and the Orderly Payment of Debts program at the Nova Scotia Department of Business and Consumer Services, all receive inquiries from people facing foreclosure[78]. They confirm that borrowers are uncertain about their position and the process which follows the notice of foreclosure. Some borrowers do not understand the documents and tend to discard them. Many do not appreciate the seriousness of not dealing with the situation. Others have a misunderstanding about their options and believe they may be able to correct a default by making partial payments. Many do not know that on default the entire principal sum of the mortgage becomes due and payable (as a result of the "acceleration clause" in the mortgage agreement). Once borrowers realize they are about to lose their home, many do not realize that they can stop the foreclosure process and reinstate the mortgage by paying all outstanding arrears prior to the initial court order being granted[79]. Borrowers may also not understand their right to redeem the mortgage, by paying the full amount owing, before the property is sold by the Sheriff[80].

It is believed information regarding default is most useful at the time of default. It is therefore recommended that legislation provide for a Notice of Default, written in plain language, specifying the rights and obligations of the borrower and outlining the steps to take to remedy the default. This Notice would replace the demand letter. It would clearly state and explain the borrower's right to (a) reinstate the mortgage prior to the court order being granted by paying arrears and related expenses and (b) redeem the property prior to the property being sold to a third party by paying the total amount owed under the mortgage.

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[78] In response, the Public Legal Education Society of Nova Scotia has prepared, in draft form, a brochure entitled "Foreclosure". It has not yet been finalized and the Society may await the outcome of the Commission's work before concluding it. The draft brochure is fairly comprehensive and includes a plain language definition of foreclosure, defences a borrower may have, how to stop the foreclosure process, the details of a Sheriff's sale and the right of a lender to apply for a deficiency judgment.

[79] Section 42 of the *Judicature Act*, *supra* note 16.

[80] *Supra* note 17.

The Commission suggests:

There is a need to make the mortgage foreclosure process clearer to borrowers. Reform should include provisions requiring a Notice of Default to borrowers, written in plain language. Among other things, the Notice would outline the rights and obligations of the borrower, the steps necessary to remedy the default and advise that (a) the mortgage could be reinstated by the borrower paying arrears and related expenses prior to the court order being granted and (b) the property can be redeemed by paying the total amount owed under the mortgage, prior to a sale to a third party.

5. Should lenders be allowed to purchase the property?

Under the Commission's proposed "modified judicial sale" process, the right of the lender to purchase the property would only arise if there is equity in the property and it is put on the market for an initial listing period. The Commission believes that during this period, a lender should only be permitted to buy the property with the consent of the borrower and subsequent encumbrancers. This option may be proposed by the parties themselves as the best solution. Any purchase by the lender would have to be approved by the court. If the lender purchased the property, it would do so at the appraised value or at a price agreed upon by the borrower.

The Commission suggests:

Lenders should be allowed to purchase the property during the intitial listing period with the consent of the borrower and court approval. A purchase at a value other than the appraised value would have to be agreed upon by the borrower.

6. Should deficiency judgments continue to be available?

The case for abolishing deficiency judgements in Nova Scotia does not seem strong. Land values are not subject to sudden fluctuations and deficiency judgments do not threaten any particular segment of the economy[81]. In order to determine whether deficiency judgments should be restricted more than they are at present, it is necessary to ask what function they serve. Their main goal is to ensure the lender is protected from any decline in the value of the land given as

[81] In Alberta and Saskatchewan deficiency judgments are not permitted against individuals, with certain exceptions. These protections date from the 1930s when depression conditions led to widespread economic failures in the agricultural community. Both of these provinces have experienced extreme variability in land prices at the various points in their histories. The Alberta Law Reform Commission recommended in 1994 that the protection be retained, because no strong policy reasons existed for change.

security. Given that such fluctuations are largely beyond the influence of both the lender and borrower, it remains to ask who should bear the risk of loss in such cases.[82] If financial institutions are always asked to bear the loss, arguably the cost of credit will rise. If consumers are always asked to bear the loss, financial institutions are insulated from the major risk of the business in which they engage. An approach which seems to apportion these risks between borrowers and lenders would seem appropriate.

The Commission's study of foreclosure files showed that nearly half of the deficiency judgments granted were for amounts less than $20,000 while 13% were for more than $250,000. The data is not available to determine the extent to which money was collected under the judgments. Anecdotal information suggests deficiency judgments are often not enforced at all or that much less than face value is recovered.

A possible option for reform is abolishing deficiency judgments for "small" amounts or setting a ceiling on the amount of a deficiency judgment, for example, as a percentage of the original mortgage loan. The former would have the advantage of economizing on judicial time where relatively small amounts are in dispute. It would also spread these losses among a number of lenders. The latter would act as an encouragement to good lending practices in that the lender would know in advance that it would suffer some exposure beyond a certain decline in the value of the property.

The Commission suggests:

That deficiency judgments continue to be available but invites further comment on whether they should be limited in some way. One option is to limit deficiency judgments to a percentage of the original mortgage loan.

7. Should changes be made through legislation?

The Commission believes changes should be made through legislation. Changes to the law of foreclosure in recent years have taken place by way of amendments to the Civil Procedure Rules and Practice Memorandum. It is perceived these changes do not receive the kind of scrutiny and public debate that precedes the adoption of legislation. It is also believed it is inappropriate to make major changes to substantive law by way of amendments to the Rules. Amendments to the Rules may be made in conjunction with legislation but should not be a substitute for legislation.

[82] In *CIBC Mortgage Corp.* v. *Levert* (1994), 135 N.S.R. (2d) 1 (S.C.), the court held it was unfair for the borrower to bear the decrease in the value of the property. While the borrower had allowed the property to fall into disrepair and cause tenancies to lapse, the overall rental market had declined and it was not fair for the borrower to bear the further decrease in value up to the time of the resale.

The Commission suggests:

Reform should be accomplished through legislation although amendments to the Civil Procedure Rules and Practice Memorandum may also be required.

IV SUMMARY OF SUGGESTIONS

The Commission suggests that:

1. The law relating to mortgage foreclosure and sale in Nova Scotia be reformed.

2. The current system of foreclosure and sale is unfairly balanced in favour of lenders and does not adequately protect borrowers.

3.
   - Sheriff's sales be abolished and replaced with a sale on the open market, depending on whether there is equity in the property at the time of foreclosure.

   - If there is equity in the property, it would be listed with a real estate agent. If the property did not sell, the lender could either accept the property in full satisfaction of the debt or surrender the property to subsequent encumbrancers (in order of priority) and sue the borrower for the full amount owing.

   - If there is no equity in the property, a foreclosure order could be issued immediately and the lender could apply for a deficiency judgement based on the appraised value. If the lender did not wish to accept the property, it could surrender it to subsequent encumbrancers (in order of priority) and sue the borrower for the full amount owing.

4. There is a need to make the mortgage foreclosure process clearer to borrowers. Reform should include provisions requiring a Notice of Default to borrowers, written in plain language. Among other things, the Notice would outline the rights and obligations of the borrower, the steps necessary to remedy the default and advise that (a) the mortgage could be reinstated by the borrower paying arrears and related expenses prior to the court order being granted and (b) the property can be redeemed by paying the total amount owed under the mortgage, prior to a sale to a third party.

5. Lenders should be allowed to purchase the property during the intitial listing period with the consent of the borrower and court approval. A purchase at a value other than the appraised value would have to be agreed upon by the borrower.

6. That deficiency judgments continue to be available but invites further comment on whether they should be limited in some way. One option is to limit deficiency judgments to a percentage of the original mortgage loan.

7. Reform should be accomplished through legislation although amendments to the Civil Procedure Rules and Practice Memorandum may also be required.