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Mr. James Rajotte

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● (0900)

[*English*]

The Chair (Mr. James Rajotte (Edmonton—Leduc, CPC)): I call the 15th meeting of the Standing Committee on Finance to order. Pursuant to Standing Order 108(2), we are continuing our study on measures to enhance credit availability and the stability of the Canadian financial system.

We are scheduled to have four organizations with us here this morning. We have three here and we're awaiting the fourth.

From the Canada Mortgage and Housing Corporation, we have the vice-president of insurance product and business development, Mr. Pierre Serré, and the treasurer, Mr. Mark Chamie. From the Canadian Foundation for Economic Education, we have Mr. Gary Rabbior, the president. As an individual we have Mr. Ian Lee, MBA program director for the Sprott School of Business from Carleton University.

We are expecting Option consommateurs.

We will begin with CMHC. We'll have a five-minute opening presentation from each organization and then we'll go to questions from members.

Mr. Serré, will you begin?

Mr. Pierre Serré (Vice-President, Insurance Product and Business Development, Canada Mortgage and Housing Corporation): Thank you.

It's my pleasure to provide the committee with information on the activities of the Canada Mortgage and Housing Corporation this morning.

[*Translation*]

Most Canadians know us through our mortgage insurance business. Over the years, we've helped millions of people to obtain a mortgage, buy a home and benefit from lower financing costs. As you know, we compete in the marketplace with private insurers, but we do so with a clear public policy mandate.

[*English*]

In 2008, over 40% of our business assisted Canadians who live in areas or in certain types of housing that are less well-served by the private sector or not served at all. This includes homes in rural areas, northern Canada, and single-industry towns. In fact, CMHC is Canada's only provider of mortgage loan insurance for mobile homes and large rental projects, including nursing and retirement homes.

Even though the economic situation is contributing to a slowdown in the housing sector, Canada's system of home financing is continuing to operate. In many countries it has become very difficult for mortgage lenders to raise funds. This hasn't happened in Canada. This is partly because of CMHC's long-standing Canada mortgage bond, the CMB, and the NHA mortgaged-backed securities programs.

The popularity of CMHC's CMB and mortgage-backed securities programs increased as the liquidity crisis deepened. In 2008, $43.5 billion worth of CMBs were issued, in addition to $61 billion worth of NHA mortgage-backed securities.

[*Translation*]

A 2008 Program Evaluation concluded that CMHC's Canada Mortgage Bond Program played a stabilizing role in Canadian markets by providing a reliable and cost-effective source of funding for mortgages. The program also provided smaller lenders with funding options. This benefits consumers by promoting competition in the mortgage market.

[*English*]

The Government of Canada also took action recently by introducing the insured mortgage purchase program, also managed by CMHC. This program is providing further support to lenders. Under it, CMHC has purchased over $53 billion to date and can purchase up to $125 billion of insured mortgage pools. In fact another auction is being held today. This provides lenders with stable long-term financing and allows them to continue lending to Canadian consumers and businesses.

[*Translation*]

Another reason for the relative stability in Canada's mortgage system, especially compared to the United States, is that Canada has a history of prudent home financing. At the peak, in 2006, sub-prime lending represented about 40% of mortgage originations in the U.S. In Canada, sub-prime lending made up only 5% of mortgages. And compared to the types of exotic mortgage products offered in the U. S., it would be more accurate to refer to the Canadian sub-prime market as “near-prime”.

● (0905)

[*English*]

In our actions we're committed to sound risk management and prudent financial practices. We do not believe it is to anyone's benefit to put Canadians into homes they cannot afford.

The government, through CMHC, is also strengthening its commitment to assist those in need of affordable housing. In September 2008 the government committed more than $1.9 billion over the next five years for housing and homelessness programs.

[*Translation*]

Canada's Economic Action Plan builds on this with an additional one-time investment of more than $2 billion, over two years, in new and existing social housing.

[*English*]

The federal government currently spends $1.7 billion annually in support of approximately 630,000 social housing households. However, a considerable portion of this housing is getting older and is in need of major repairs and upgrading. The $2 billion investment in the action plan includes $1 billion for the renovation of this important national asset. It also includes significant funding for housing in first nations and northern communities, for seniors, and for persons with disabilities.

Canada's economic action plan also commits $2 billion for low-cost loans to municipalities to assist them in undertaking housing-related infrastructure. Municipal governments will be able to complete straightforward loan applications on CMHC's website and receive quick responses to their applications.

In closing, I want to assure the committee that in all of our activities, CMHC is committed to fulfilling its policy mandate while exercising prudent financial management and conducting proper due diligence.

[*Translation*]

I would like to thank the committee, and we would be pleased to answer your questions.

Thank you.

[*English*]

The Chair: Thank you very much for your presentation.

We'll go now to Mr. Rabbior.

Mr. Gary Rabbior (President, Canadian Foundation for Economic Education): I would like to extend my thanks to the committee for the invitation to appear before you today.

The Canadian Foundation for Economic Education, or CFEE, as we're affectionately known, is a national, charitable, non-partisan organization working to try to improve economic and financial literacy among Canadians. Founded in 1974, the foundation works with schools, ministries, departments of education, community service agencies, immigrant-serving agencies, and many others to try to improve the economic and financial capability of Canadians. Our goal is to help Canadians plan for and build a successful economic future.

We've had some success over the years, but not as much as we'd like, and not as much as what lies as the potential for success today. The current downturn has created an unprecedented interest in the need to improve economic and financial literacy. It is an opportunity that we feel must be exploited.

Today, virtually all Canadians have been affected by the economic downturn. Economic recovery, when it comes, will likely bring with it increased complacency and more acceptance of what has been a less than ideal status quo. When times improve and the impact of hardship is less widespread, concern and interest will likely diminish. The time is right to initiate efforts to improve economic and financial literacy and level the opportunity playing field in Canada.

I know that many eminent representatives have appeared before you, individuals representing financial institutions, government departments and agencies, industry associations and others, but I would like to try to speak as best I can for the many average Canadians who will not have this opportunity. I would like to try to give a voice, if I can, as best I can, to their interests, their concerns, and their hopes for the future.

In that regard, we believe Canadians aim to act rationally. It is not their desire to dig themselves into financial holes, suffer the financial anxieties of over-indebtedness, have relationships that suffer from financial stress, and see their hopes for the future diminished. For the most part, Canadians are simply trying to build a successful future for themselves and for their families. In doing so, their decisions and actions are affected by many things.

Two factors are especially significant: first, the knowledge and skills they possess; and second, the incentives that influence their decisions and actions, by which I mean the prospects of reward or benefit, or the risk of penalty or punishment. If we want behaviour to change in the future, increasing knowledge and skills will not be sufficient. Our incentive structure, which comes from policies, regulations, programs and statutes, will also need to change.

Consider an example. Most agree that the economic crisis started in the United States, triggered by the subprime lending methods that spread like a virus around the world. Part of the blame is often placed on the so-called foolish people who put no money down on a home, borrowed at low but soon to be higher interest rates, and soon found themselves unable to carry the cost of a home that was now worth less than their mortgage.

Were these people really so foolish, or did they act in a rational way? They, like most of us, held out the hope for a home for their family. The system of rules, regulations, and incentives in place basically reinforced the idea that everyone should be able to realize that hope. So many people bought a home with no money down, as 43% of Americans who bought a home in 2005 did. They took out 40-year mortgages that lowered their monthly costs but dramatically increased the total cost of their home. They believed they could afford the start-up teaser payments, which are low in the first few months, and come to fulfill their dream and put their family in a home.

The reality is that many probably could not afford that home, but the regulations, policies, and programs in place led them to believe they could and enabled them to do so. Without adequate economic and financial knowledge and skills, they jumped into the market, a dive into a pool that would come to be plagued with problems.

What factors were at work leading Canadians to make the decisions they did over the last couple of decades? Do we believe that the past decisions and actions of Canadians created conditions of risk and instability in our financial system and in the lives of Canadians? To answer that question, consider some of the statistics that define the path leading up to the realities of today.

Since 1996, Canadians have spent virtually all of their income. By 2005, for each dollar of disposable income that Canadians had, they owed $1.16. The savings rates for Canadians peaked in 1982 at 20.2%; by 1990, the savings rate was 1.9%; at the start of the downturn it was less than zero. The per capita debt of Canadians rose 5.2 times over the last 25 years, from $5,470 in 1980 to $23,390 in 2005. Between 1982 and 2001, the total amount owed by Canadian households rose 152%, while disposable income grew by 42%. Canada's household debt-to-income ratio went from 55% in 1983 to 105% in 2003. Only one in three Canadians expecting to retire in 2030 is saving at levels that will be required to meet basic household expenses. The proportion of Canadians covered by company pensions had fallen to 39% in 2003, a decline from 45% in 1991. And it continues to fall.

● (0910)

The statistics could go on, but I'll share with you the last one I have on my list. The fastest-growing company in Canada, according to the June 2007 issue of *Profit* magazine, was Rentcash in Edmonton, Alberta, with a growth rate of 33,700%. Revenues for the company grew from $456,000 in 2001 to $154 million in 2006.

I'm going to skip ahead a bit. I'm just letting the translators know that.

Canadians, therefore, need help now. This was made very evident in the first national survey of economic and financial capability that CFEE undertook recently with The Strategic Counsel. The results are posted on CFEE's website. I brought along a copy of the survey results for the committee, if there's interest.

Canadians are looking for help now and they need help now. They are willing to seek it out from sources they can trust, from sources that are able to provide help in ways that people can understand and can relate to their life circumstances and challenges.

I've brought along a couple of resources, which I've shared with you. The *Money and Youth* publication has over 300,000 copies in circulation. Our *Newcomers to Canada DayPlanner*, at more than 400,000 copies, is in its ninth printing in just over two and a half years.

Canadians are desperate for resources to help them with their economic and financial understanding, especially if it is in clear, layperson terms, something we have a big problem with on the supply side of the financial marketplace today.

We would also like you to be aware that the foundation and its many partners and supporters and volunteers stand ready to support the work of the government and this committee, if there is any way in which you think we can exist. There is so much being done, and much more that can be done, to try to ensure that Canadians have the best opportunity they can have to build a successful economic future.

One thing we need to do is to somehow develop a consensus guideline for what actually constitutes economic and financial literacy so that we can all begin to work together toward similar goals. There's so much we can do, and so much we should be doing, to build a national strategy. I commend the government for its task force. However, at the same time, I'm not sure we need two years to put an action plan together. I'm not sure we can afford two years to put an action plan together. I think we need to do something now.

Thank you very much.

The Chair: Thank you for your presentation.

We'll go now to Mr. Lee, please.

Professor Ian Lee (MBA Program Director, Sprott School of Business, Carleton University, As an Individual): I'd like to thank the committee for inviting me. I'd also like to thank Mr. Pagé and his able staff for supporting me at the last minute with translation.

I am the MBA program director at the Sprott School of Business. However, throughout the seventies and early eighties I was the loan manager, mortgage manager, and commercial credit officer directly across the street from the West Block in the Bank of Montreal building. It was the fourth largest branch of the Bank of Montreal. At the time, we had $200 million in mortgages. I lent millions of dollars in conventional and high-ratio mortgages across this city.

The PowerPoint presentation that I'm going to give is based on an article I have almost completed and have partially presented at a couple of academic conferences.

Before I go into the proposals I'm going to recommend today, I really want to give you their context.

I am arguing in this article that the housing bubble, housing collapse, and financial crisis were due to a government and policy failure in the U.S. Congress. The Congress micro-managed the banks, but did not provide oversight and supervision. They refused to regulate the shadow banking system, and as a consequence, I'm arguing—and I don't know anyone else who has made this argument—commercial banks, populated by highly intelligent people, understood they were being forced by Fannie Mae and Freddie Mac to make a lot of bad mortgages. So they used securitization to dump those junk mortgages on other people to get the mortgages off their books. This lead to the housing bubble and collapse and the financial crisis. There is massive empirical documentation for this.

Most of my slides are graphs, so I can go quite quickly.

This slide shows the percentage of low-documentation or no-documentation mortgages. You can see that by 2005, 2006, and 2007, over half of all mortgages in the United States of America were low-doc or no-doc ones, popularly called NINJA mortgages: no income, no job, no assets.

Some hon. members: Oh, oh!

Prof. Ian Lee: In terms of the dollars, you can see that the subprime and Alt-A mortgages.... For those of you who don't know, Alt-A mortgages are just above subprime mortgages but are below prime ones. So about 55% of all mortgages written in 2004-05 and 2005-06 were junk mortgages or bad mortgages that should never, ever have been written.

I draw your attention to the right-hand graph, which shows the securitization. The yellow is for subprime and the green is for non-conforming mortgages, which is another polite word for bad mortgages. You can see they were about one half of the approximately $2 trillion in mortgages written.

What did this do? Well, as anybody who understands economics and banking would know, it drove up the home ownership rate from about 62% to 69%. In other words, millions of new buyers entered the market.

If millions of new buyers enter the market, what is that going to do? It's going to drive up house prices. During this period throughout the nineties, real incomes were flat; they were not going up. Take a look at that red line; that's average house prices. Even though incomes were not going up at all in aggregate, the house prices went almost vertical, because of these policy mistakes. As a consequence, it drove up debt service from the long-term average over a period of some 25 to 30 years of 12% up to almost 14% of income being allocated to service debt, which is unsustainable.

So this was the outcome of the bad laws and bad regulations. It was perfectly predictable. It drove up inflation. The Fed put up interest rates—which were probably too low in the first place. Secondly, it drove up mortgage delinquencies; that's the graph on the bottom right. And thirdly, home prices started to come down.

So what does this mean for Canada? The very good news is that Canada did not melt down. The argument I'm providing in the paper is, number one, that this was due to the very high quality of the human capital in the Canadian chartered banks, the strongest banking system in the world, in my judgment and according to international evaluators. Second, it should be said that Canada has been very fortunate to have had very strong Canadian regulators. I'm referring specifically to Parliament: you did not go over the cliff, as the U.S. Congress did. Also, the Department of Finance has outstanding people, as does the Bank of Canada and OSFI, the Office of the Superintendent of Financial Institutions. Finally, there is a pragmatic, small-c conservative culture amongst Canadians.

I've read the transcripts of the committee hearings and know that the committee is very concerned about bank credit and its availability and the perception that bank credit granting has declined. In fact, empirically, factually or statistically, it has not. Bank credit has gone up in the last year.

However, before I go to the next slide dealing with the pricing of credit, what has happened is that the so-called shadow banking sector has collapsed and is not lending. So there's less credit being granted, although the banks are doing more heavy lifting.

In terms of the pricing—because some of you are very concerned about the widening spread, and David Dodge has spoken about this in his interviews and his two excellent presentations in late November—banks are recapitalizing in anticipation of loan losses, because in every recession loan losses go up, and that's going to drive up the pricing.

● (0915)

So what is not working today in Canada? The shadow or parallel banking system, which are the money funds, the asset-backed securities, the investment banks, the hedge funds, derivatives, exchange-traded or OTCs, which is over the counter, derive from something else. These are not regulated. I don't have a number for Canada, but Secretary of the Treasury Geithner estimates the shadow banking sector in the United States—this is end of 2007 data—is $10 trillion.

The regulated banking sector is $10 trillion. In other words, the shadow banking in the States was about 50% of the total. That figure corresponds to that of Canada. The Bank of Canada estimates that banks make up 55%, so shadow banking is somewhere around 45%. Almost one-half of the financial system in Canada is not regulated. In other words, there is no recourse for assets, there is no transparency, and there are spurious credit ratings.

MPs are worried about the decline in credit. Yet the shadow banking provided about half of all the loans. But the shadow bankers withdrew because of the financial crisis. I argue they withdrew because they were overleveraged. They were overleveraged because they were not regulated. Now is the time to solve the problem by supporting a national securities regulator. How do you deal with the question of solving the declining availability of credit? For 25 to 30 years banks have wanted to lease cars, and this was opposed by the dealers' association. I was in a bank when they were opposing it. Now the chickens are coming home to roost for them because the acceptance companies, such as GMAC and Chrysler Credit, have pulled out. There's insufficient credit.

Parliament has an opportunity to resolve this by authorizing direct bank leasing in the branches.

These are my last two slides. My recommended policies are: one, approve and establish a national securities regulator to include the regulation of the shadow banking system; two, authorize banks to lease through branches; three, modify mark-to-market accounting rules to eliminate pro-cyclicality, which David Dodge has spoken about as well; four, maintain the OSFI raw leverage ratio at 20:1; five—I argue, with all due respect to the people from CMHC, that we have a problem in Canada—CMHC should be more regulated because they have two businesses in one and they're not regulated by OSFI or some similar agency, and David Dodge has also spoken about this; six, you have to create a clearing house for credit swaps; and finally, I support the lending program, the extraordinary financing program announced in the budget, as there are very imaginative, innovative, and prudent ways to partially address this problem.

Thank you.

● (0920)

The Chair: Thank you very much, Mr. Lee, for your presentation.

We'll go to our fourth group now, Options consommateurs.

Monsieur Arnold, you will be presenting on their behalf.

[*Translation*]

Mr. Michel Arnold (Executive Director, Option consommateurs): Mr. Chairman and members, it is my turn to thank you for inviting us to present our comments and recommendations regarding the government assistance to the Canadian financial sector, particularly with respect to access to credit for individuals, the protection of savings and the stability of the Canadian financial system.

This is not the first time that we have appeared before this committee, and I will bet that this will not be the last time either. For those of you who are not familiar with our group, Option consommateurs is a non-profit organization headquartered in Montreal, but we also have an office in Ottawa, run by Ms. Anu Bose, who is here with me this morning. Our mission is to promote and defend the interests of consumers. Established in 1983, Option consommateurs closely follows issues pertaining to energy, agrifood, financial services and business practices.

The recession has hit the country's job market head on. According to Statistics Canada, some 129,000 people lost their jobs in January, including 30,000 in Quebec. At the same time, we are seeing a sharp increase in the number of insolvencies. No fewer than 90,000 consumers declared bankruptcy in Canada in 2008, compared to nearly 80,000 one year earlier, which represents an increase of 13.5%. These are individuals who in all likelihood will not be able to participate in the economic recovery.

In order to deal with this economic upheaval and the worsening international credit, the Government of Canada implemented the Extraordinary Financing Framework in order to enable Canadian financial institutions to continue providing access to financing to both consumers and businesses. This framework contains numerous support measures for both private and public institutions, and it would appear that Canadians have no say in the way it is being implemented, something that is essential to the democracy of this country and the confidence of consumers.

Moreover, the comments made by various keynote speakers invited to attend an international seminar that we organized on March 12 and 13, which focused on consumer credit and debt, are rather worrisome, if not downright alarming. Perhaps I am not telling you anything new when I say that, over the past 25 years, consumer debt in Canada has more than doubled, going from 15.7% of disposable personal income in 1981 to 36.2% in 2007. Not only has the amount of debt in households risen, but savings fell beneath the zero mark in 2005. According to Statistics Canada, savings were sitting at minus 0.5% in the second quarter of 2005, something not seen since the 1920s.

As far as access to credit for individuals is concerned, we now see that we have two categories of consumers: for one group, access to credit has been too easy and has quickly led to too much debt, and in the other group, access to this credit has systematically been turned down. In both cases, it is very difficult for us to know what criteria have been used by the financial institutions in their decisions to grant credit.

These observations on the government's financial assistance programs for the Canadian financial sector and on the state of finances of individuals enable us to make three recommendations. I will let Ms. Bose present these recommendations to you. We would then be pleased to answer your questions.

● (0925)

[*English*]

Mrs. Anu Bose (Head, Ottawa Office, Option consommateurs): Thank you.

These observations on the government support programs for the Canadian financial sector and on the finances of individual consumers lead us to offer three recommendations.

In order to help build consumer confidence, we recommend that the Government of Canada take care to ensure that the criteria and rules for its aid programs for the Canadian financial sector are clearly understood by all stakeholders within the financial industry, within business, and among consumers. This will allow for a well-informed discussion.

Secondly, we recommend that the Government of Canada ensure that the accountability mechanisms for financial institutions include criteria for lenders' responsibility in judging borrowers' creditworthiness.

Lastly, in light of its enhanced role in maintenance of the financial sector's stability, we recommend that the government undertake an immediate review of the Canada Deposit Insurance Corporation, CDIC, and its ability to fulfill its mandate to protect the savings of Canadians in the event of insolvency of a financial institution and that the government make public the results of its review.

Thank you very much.

The Chair: Thank you very much for your presentation.

We'll go to questions from members. We'll start with Mr. McCallum, please.

Hon. John McCallum (Markham—Unionville, Lib.): Thank you, Mr. Chair, and thank you to all the witnesses for appearing here.

I'd first like to ask a question about CMHC to Mr. Serré. It's my understanding that until 2006, the maximum length of a mortgage that CMHC would ensure was 25 years, but as of, I believe, the fall of 2006, that changed, so that for the first time CMHC would insure mortgages for up to 40 years with zero down payment. Is that correct?

I'm interested as to why this change was made. Did CMHC request that, or was it imposed on you, or how did this come to pass? It looks suspiciously like a U.S. subprime-type arrangement.

Mr. Pierre Serré: Thank you.

In terms of the 40-year amortization, that was introduced in the marketplace in October of 2006, as you said quite correctly. We came in with our offering in December, and 2006 was the year that extended amortizations were introduced. CMHC has been in the mortgage insurance business since 1954 and has always worked with its lenders, and also Canadians, to ensure that the products meet the demand.

Hon. John McCallum: No, no, that's not the question. I know you've been working since 1954. I don't have all the time in the world. Why did you go for a 40-year mortgage with no down payment?

Mr. Pierre Serré: These products, as we introduced them, are not for everyone. When we looked at the marketplace and the demand for such products, we introduced them in a prudent and very conscientious manner—

● (0930)

Hon. John McCallum: Okay.

Professor Lee, I notice you nodding your head. You were talking about the problems with the subprime in the United States, south of the border. You were talking about how things were good here. What's your interpretation as to whether it was a good idea to introduce this, and if you have any knowledge, why do you think they did it?

Prof. Ian Lee: I thought it was a terrible idea. I thought it indicated at that point why CMHC needs to be regulated by another authority, perhaps the Superintendent of Financial Institutions. I think any mortgage insurance company that will go to zero down or a 40-year amortization has demonstrated that they do not understand the mortgage market.

Any mortgage manager or person who makes mortgages will tell you that when you get below 10% down, you are getting into very dangerous territory, because, to use the slang, the owner doesn't have any skin in the game. That is to say, when you approach zero, your risk is going up exponentially, and it is very dangerous. They should never ever have done it.

Hon. John McCallum: Thank you. That's my sentiment too.

Mr. Serré, can you tell us the value of mortgages insured at 40 years and zero down payment, and how many there are?

Mr. Pierre Serré: Yes, I can, but just to make it clear, the 100% mortgages weren't offered to anybody.

Hon. John McCallum: I know, but please, I don't have much time. What is the value of the mortgages issued at 40 years and zero down payment?

Mr. Pierre Serré: If you take a look at our outstanding insurance in force, all the mortgages that CMHC has insured, the percentage of all of the mortgages we have insured that would be either 40-year amortization or 100%—one or the other—would be about 8%.

Hon. John McCallum: That's 8%. Do you have any idea as to what proportion of those may have gone sour?

Mr. Pierre Serré: We monitor our arrears rate in the same manner as the CBA reports its arrears rate, and our trend lines are very similar to the Canadian Bankers Association—

Hon. John McCallum: But that wasn't my question. Of the 40-year, zero down mortgages, do you have any idea how those particular mortgages are faring in terms of being in good shape financially or not?

Mr. Pierre Serré: I can't disclose all of the details of all the different product lines, but they are not performing dissimilar to what our expectations were when we launched them in the marketplace at the premiums they were launched at back in 2006.

Hon. John McCallum: Okay.

On another subject, Professor Lee, you quoted David Dodge. I'm also a fan of David Dodge. I think he's a gift to Canada in terms of his ability and experience, including his statement of last week. He proposed counter-cyclical mortgage rules, such that when housing prices are rising fast, conditions be tightened, and in a slump they be loosened. What do you think of that proposal?

Prof. Ian Lee: I completely endorse it. My criticism was at the micro-end, if you will; that is, at the individual mortgage end. You're facilitating huge increases in losses. David Dodge's criticism is at the macroeconomic end, and it is also very compelling. He's saying that by reducing the down payment required when the economy is rising and charging forward, you're throwing gasoline on the fire and making the economy move towards if not hyper-inflation then much stronger inflation, and you should be doing exactly the opposite at that period. I completely agree with David Dodge.

Hon. John McCallum: So do I, and I think, as you just said, the two things are not incompatible. You want prudence in terms of not having these 40-year, no down payment mortgages, but at the same time the conditions could vary counter-cyclically for macro reasons, right?

Prof. Ian Lee: Absolutely. In fact, David Dodge suggested that and urged that, and that is one of the things I'm recommending to the committee, and that's why I think CMHC needs outside scrutiny by a government agency such as OSFI.

Hon. John McCallum: Thank you very much.

The Chair: Thank you, Mr. McCallum.

We'll go to Mr. Laforest.

[*Translation*]

Mr. Jean-Yves Laforest (Saint-Maurice—Champlain, BQ): Thank you, Mr. Chairman.

Good morning to everyone.

My first question is for Mr. Arnold and Ms. Bose.

At the end of your intervention, you made some recommendations that we have not often heard at the Standing Committee on Finance. I find your recommendations particularly interesting. You represent consumers who, in the final analysis, are the hardest hit by the current crisis. These are the people who are losing their jobs and dealing with major credit problems. In addition, they're the first ones to be stung, either by banks or businesses offering various consumer items and advertizing in an effort to get their money.

It is clear that you want the government to define clear rules for the government itself and banking and financial institutions that receive assistance. I find that quite relevant. There is also another side to the coin. There should be accountability rules for consumers. Did I understand you correctly?

● (0935)

Mr. Michel Arnold: We represent consumers but we also represent taxpayers. So we think that the $75 billion that has been loaned and the guarantees provided to the banks come from taxpayers' pockets. Accordingly, we are asking for transparent rules regarding these various programs and we are also asking that the institutions that benefit from this assistance comply with a clearly established accountability process that is in the public domain so that consumers, individuals, can be aware of the rules and, if need be, be able to ensure that their rights are being respected under these same rules. That, essentially, is what our message is all about.

Mr. Jean-Yves Laforest: The third recommendation pertains to some type of support from the government.

Mr. Michel Arnold: We are recommending that the government ensure that the Canada Deposit Insurance Corporation have the means to ensure that investors are protected should these financial institutions go bankrupt.

Mr. Jean-Yves Laforest: Thank you very much.

I have a question for Mr. Lee.

In your testimony, you compared what happened in the United States to what happened in Canada. Based on what you have said, Canada was protected by a number of systems, in a way. You referred to the Department of Finance, the government, members, to almost everyone, actually. Everything seems fine and dandy in Canada, even the regulatory system.

However, further on you recommend that there be one single securities commission. Well, you must know that that is an area of provincial jurisdiction, and that has always been the case. In other words, you are prepared to see the government engaged in a constitutional war. You know that in Quebec, there was a great outcry in reaction to the government's expressed intention. Do you think it would be productive to go that route? We have got good performance, but you want to stir things up, at the risk of creating a furor. In fact, it is already the case. I'm having a hard time understanding your arguments.

Could you give me further explanations?

[*English*]

Prof. Ian Lee: I'd be pleased to.

First, I'm certainly not, and I don't think anyone else is, advocating a constitutional battle by forcing it on any province. It will be a voluntary proposal, and those provinces that want to joint in will because it is in their self-interest. That's the first argument.

In terms of the underlying logic of why we should do it, we are the only country in the G-7, and I believe the only country in the G-20, that does not have—let's be blunt—a grown-up, mature, sophisticated financial regulatory system. We have 13 provincial regulatory systems—

[*Translation*]

Mr. Jean-Yves Laforest: You said that Canada was the only country in the G7 or even in the G20 that did not have this type of regulatory system in place, but that in the U.S. there was a single system. Well sir, it has not worked. We all agree that this crisis started in the U.S. The system did not prevent the major problem we now have from occurring, the current recession. For one thing, there is the issue of bad debt related to mortgage loans. You yourself demonstrate in your document that things did not go well in the United States where there is a single regulator.

● (0940)

[*English*]

The Chair: Mr. Lee, just a brief response, please.

Prof. Ian Lee: Okay.

I want to, if you will, correct you. I did not say it was due to the SEC; I said it was due to Congress, who failed, in fact encouraged, Fannie and Freddie to go over the cliff in making mortgages that should never have been made.

But in terms of the larger issue, Paul Krugman has noted accurately that many of the failures in the financial markets occurred in the shadow banking sector that is *not* regulated. So the problem is not that there was a failure of regulation, it was a failure of the *absence* of regulation.

The Chair: Okay.

Merci, Monsieur Laforest.

We'll go to Mr. Menzies, please.

Mr. Ted Menzies (Macleod, CPC): Thank you, Mr. Chair.

Thank you to our witnesses for enlightening us on some very interesting discussions that we've started on our access to credit process at this committee. My first question might be to flesh out some of the answers that weren't quite finished by Monsieur Serré. I know Mr. McCallum was quite focused on what he wanted his answers to be, and I know you were trying to get in a bit of an explanation.

Please clarify for us if you can, could you have a 40-year mortgage at 100%? We removed that in July. You can confirm that for us, if you would.

You had suggested that 8% of those 40-year mortgages.... I think we need to note that comparison of 8% with the statement by Mr. Lee that nearly 60% of the mortgages in the U.S. were subprime or near prime. We recognized the uncertainty in that and got rid of it.

So perhaps you could finish the answers that Mr. McCallum wouldn't provide you the opportunity to.

Mr. Pierre Serré: Thank you.

In terms of the 8%, yes, in fact that includes people who had either 40 years or 100%, and in some cases they would have had 40 years and 100%. But again, just to be clear on the 100%, there was a minimum requirement on that, which meant that people really had to demonstrate proven behaviour in managing their debt in the past in order to access that.

Mr. Ted Menzies: So that would be different from a U.S. subprime?

Mr. Pierre Serré: That is exactly where I was heading. From our perspective, the subprime is characterized by a lack of creditworthiness on behalf of the borrowers. For all of our products, including 40-year amortizations, and especially on 100%—because we're very careful in introducing and managing that one—we had stringent requirements for creditworthiness, which, by definition, means that these types of products were not subprime.

Comparing it to the U.S. is extremely difficult in that what happens in the U.S. is very different from what happens in Canada. The systems are completely different, right from the mortgage interest being deductible to other significant parts of the process. Comparing one to the other is very difficult.

Mr. Ted Menzies: Thank you.

I might also mention that in a number of our pre-budget submissions that we had in the lead-up to this budget, Canadians were still recommending mortgage deductibility, despite what has happened. So I guess that just goes back to financial literacy, people not understanding what got the financial institutions and homeowners in trouble in the U.S.

Mr. Pierre Serré: Perhaps I could add that also in Canada we don't have non-recourse lending as they have in many states in the U.S. That makes a big difference. Canadians don't want to lose their homes. They don't buy a home in order to lose it, nor do the lenders or the insurers put people in that position.

Mr. Ted Menzies: Good.

Mr. Lee raised some concerns with CMHC. We want to be certain that you have the required oversight or that there is required oversight over CMHC. You will be delivering a large amount of our extraordinary financial framework through the $125 billion in this insured mortgage program. I see there's another offering again today. The last offering was not completely taken up. Can you provide a bit of reassurance to this committee on how that's going to be handled and whether the proper instruments are in place to make sure that's handled properly?

● (0945)

Mr. Pierre Serré: Are you referring to IMPP itself?

Mr. Ted Menzies: Yes.

Mr. Pierre Serré: Maybe just as a preamble to that, I will say that we are a crown corporation. As set out in the Financial Administration Act, there's a very stringent regulatory framework that governs us, including annual audits by the Office of the Auditor General, as well as a special examination every five years of all of our systems and practices at CMHC. From a mortgage insurance perspective, we have external actuaries that opine on the adequacy of all of our reserves every year, so there is in fact a very stringent regulatory process in place for us as a crown corporation.

While we're not regulated by OSFI, by virtue of being a crown corporation not existing under any acts that OSFI regulates, we do follow their capital requirements with regard to mortgage insurance. In order to conduct our business properly, we capitalize ourselves and have the same systems and practices that a private mortgage insurer would have. Really, that's one of the things that underpins, I guess, the insured mortgage purchase program, in that all of the mortgages purchased through that program are already insured. That insurance is provided either by CMHC, which follows OSFI, or by private mortgage insurers, which are regulated by OSFI.

So already in terms of comfort to this committee, the established procedures are stringent, and the IMPP is only able to purchase already insured mortgages. As the committee knows, there's government backing of those mortgages. There's no purchase in that program of non-government-backed insured mortgages.

Mr. Ted Menzies: Thank you.

The Chair: You have one minute.

Mr. Ted Menzies: Just to follow up on some comments of Mr. Rabbior over Rentcash, I know you're picking out one individual corporation, but I have a quick comment. We're looking at financial literacy. What do we do to make Canadians aware that there are better ways to get a hold of cash than through some of these facilities that are taking advantage of Canadians?

Mr. Gary Rabbior: Part of the problem is that increasingly as a society we're transferring more and more responsibility to Canadians for their financial decisions. They're planning for their retirement, paying for their kids' education, and managing their debt, yet at the same time we didn't do anything particular through our education system to prepare Canadians for the responsibilities that they're increasingly having to assume. We're paying a price for that now.

I'm pleased to say Manitoba has just agreed to collaborate with us to integrate compulsory economic and financial education into their core curriculum. We're in discussions with Ontario right now to do the same. We're hoping to have discussions with other provinces. So increasingly, there's a chance to build for the future.

Right now, one of the things the U.K. is doing is setting up a national network of what they're calling “financial guidance”—non-profit guidance that British people can go to and get help from in understanding their financial affairs before they go to commercial companies for their financial products. To my mind, there are many Canadians out there who are desperately trying to understand the financial products being offered to them in increasingly complicated language. As well, the products are becoming more complicated. Even Tony Fell and Ed Clark, from the TV, have admitted that they haven't been able to understand some of the products that have come their way and they therefore haven't offered them to clients. That's part of the challenge we face.

The Chair: Thank you.

Thank you, Mr. Menzies.

We'll go to Monsieur Mulcair.

[*Translation*]

Mr. Thomas Mulcair (Outremont, NDP): Thank you, Mr. Chairman.

I would like to thank Mr. Serré for nuancing his response appropriately. Mr. McCallum seemed to be in quite a rush to ask a number of questions without giving Mr. Serré the opportunity to respond in full. Well, these nuances needed to be made, given the circumstances. There is a huge difference between the situation in Canada and that in the U.S.

Nevertheless, I would like to ask Mr. Serré a question on this point. At this point in Quebec, some financial institutions, including the Mouvement Desjardins, are offering open mortgages at a 1% or 1.5% rate. That happens frequently. However, if people want to convert them into closed mortgages for a four- or five-year period, the interest rate is rather high when compared with the market rate, in other words 6% or 7%.

Is your organization currently looking into this situation? I am less concerned about a 40-year mortgage or a 0% rate, for the reasons suggested by Mr. Serré, than I am about the 1% or 1.5% rate. Oftentimes, and that was implicit in Mr. Arnold's comments, people who are purchasing homes are less concerned about price than they are about monthly payments. That is what concerns me somewhat. Are you following the situation? Is this something you would normally be concerned with?

● (0950)

Mr. Pierre Serré: Thank you for your question.

That is not something that we follow closely from one day to the next. Rather, it is governed by competition among lenders in the mortgage market. We mainly deal with loan-value ratios over 80% in the market. Borrowers generally opt for fixed rates. Certainly, buyers prefer fixed rates for the first term.

This is not something we examine in great detail. However, we see that the market managed the issue through competition among lenders.

Mr. Thomas Mulcair: Let's face the fact that the only way to reimburse trillions of dollars is through inflation. If we were to draw a lesson from the Vietnam war, which ended in 1975, we'd see that the only way to pay down the debt was through inflation in the late 1970s and the early 1980s. We are going to go through the same thing. The only way to reimburse the trillions of dollars that went into the Iraq war, based on the way in which the United States is trying to absorb the “toxic debt”, would be through inflation.

Do you not fear the worst, if we were to allow a large number of variable rate mortgages at 1% or 1.5%? If, all of a sudden, the rate were to rise to 13%, which is far from unthinkable, would we not be creating our own sub-prime crisis? Not for the reasons raised by Mr. McCallum, but rather because we would have granted too much credit to people attracted by rates which are simply unsustainable.

Mr. Pierre Serré: That is speculation. To my knowledge, borrowers always have the opportunity to convert their variable rate into a fixed rate in difficult times.

Mr. Thomas Mulcair: If at first you are offered a variable rate of 1.5% and then it jumps to 8%, it does make a slight difference in your monthly payments.

Mr. Pierre Serré: Absolutely, but I'm not sure it is such a...

Mr. Thomas Mulcair: The difference is already in that order. You can get a 1% or 1.5% rate, but if you try to set it for five years you get a 6% or 7% rate. That is the situation today.

Mr. Lee, I would like to get back to a point you raised earlier on with respect to the mark-to-market accounting rule. Four or five weeks ago, when the United States was considering striking this rule, did you see the stock markets skyrocket, as we did? You are a university professor. In your opinion would that support the striking of this rule or is it not rather an indication of the fact that the very striking of the rule is perceived as another way of making money very quickly in the market? Would we not be better advised to stabilize accounting rules over the long term by maintaining the mark-to-market practice rather than eliminating it, as you suggest?

[*English*]

Prof. Ian Lee: No, I don't support the elimination of mark-to-market accounting. It has been supported by all the major accounting bodies in the western world; FASB in the United States and CICA in Canada support it. It simply argues that assets should be valued at market value, not historic value. So in principle there's nothing wrong with that.

My and others' objection to mark-to-market accounting in a financial crisis is that you have market failure at this moment where the assets cannot be sold at any price. So any price you impose on it for recognition on the balance sheet is arbitrary and, if you will, fictitious. It's not a real market price. To restate it, you cannot establish a market price when we're in a situation where the markets have failed, as we have right now. So the rule has to be applied prudentially and possibly even suspended at this moment, whereas in the States there is no market for many of these assets.

[*Translation*]

Mr. Thomas Mulcair: If it is already fictitious, what would be the market price?

[*English*]

Prof. Ian Lee: Currently that's precisely the point. At this moment the American price for a lot of these toxic assets cannot be established. In other words, we have what I would characterize as temporary market failure.

● (0955)

[*Translation*]

Mr. Thomas Mulcair: Then, what are you suggesting? If at this point we cannot set a price without it being fictitious, what would you propose we replace mark-to-market accounting with? What type of change are you suggesting?

[*English*]

Prof. Ian Lee: We're getting into an area called business valuation. It's a course we actually offer in my MBA program. It's a very tactical area because there are different methodologies to measure. There's replacement value, there's historic cost, there's market, and so forth.

I am not a professional accountant, but what is being proposed right now is using an estimate, a judgment by professional accountants of the corporation or organization that would look at the historic values and the current values and basically pick a price. It may sound capricious, but when you have a failed market where there is no market price, any price that is chosen is arbitrary.

The Chair: Thank you.

We'll go to Mr. McKay.

Hon. John McKay (Scarborough—Guildwood, Lib.): Mr. Chair, I want to follow along with Mr. Lee here. I take it, in effect, that this mark-to-market modification you're proposing is like a rolling valuation, and that at certain intervals, whether it's monthly, quarterly, or whatever, the folks decide this is what it's worth.

What does that mean for financial institutions in Canada?

Prof. Ian Lee: I think the impact would be far less severe in Canada than in the United States. Again, I will come back to my comments about the prudential nature of Canadian banking. And this isn't meant to be any kind of propaganda, as I don't have any relationship to the banks any longer. I don't consult to them; I don't own shares in them.

Nonetheless, the culture in Canadian banking is very different from the culture in American banking. It's much more cautious. It's much more pragmatic. It questions. Certainly on their balance sheets, if you look at their published financial statements, they do not have the kinds of losses that American banks have. Canadian banks are solvent.

So to answer your question, I think it would be much less dramatic.

Hon. John McKay: How would that then impact on the 20:1 ratio that you're proposing be maintained in your next bullet point? The reason that valuation is going down...you're going to have to put some more cash up.

Prof. Ian Lee: Indeed. I put that in because the British just released their proposal for reregulating financial services two days ago. They came out quite strongly against a raw metric. I haven't talked about this in my slides, but although the American banking situation is in very bad shape, Europe is in far, far worse shape. Their banks are running a 40:1, 50:1, 60:1 leverage. American banks are running at 28:1. We're at 18:1. We are underneath the 20:1 ratio. I don't think it would have a big impact, because again, the Canadian banks, although there is a regulatory framework, are self-regulating. They make sure they don't go right up against the limit, which is why they're at 18:1 now.

Hon. John McKay: Most of them seem to have been able to pass this basic book. I do wonder, if we sent it to some of our colleagues in the States, whether they'd be able to pass the basics there.

Whenever we've played around with banks and leasing, for all the 11 years I've been in Parliament, there's been a line-up of car dealers out that door on to Wellington Street, saying, “No, you can't do this. It's absolutely impossible.” Their basic argument is that if in fact the banks move in and lease, they will simply occupy the field and destroy the market.

What's your reaction to that?

Prof. Ian Lee: I've never bought the argument, although in the absence of any hard evidence it's difficult to say.

From the banks' perspective, they're going to charge more if they get into car leasing because they're not doing it to provide incentives to the consumer to buy a car. They're doing it because it's a financial product on which they want to make money, just like any other financial product, whereas the acceptance companies—and by that I mean General Motors Acceptance and the Honda acceptance company and so forth—are a captive arm of the automotive manufacturer and they're trying to move cars.

I've never understood the dealers' criticism, because they will get better rates and they control who they put the deal through at the dealership.

Hon. John McKay: Doesn't that mix your portfolio? The banks pick up the cream and leave the junk to the acceptance corporations. The acceptance corporations are then going to be under some pressure to refinance themselves. Doesn't that put GMAC and the Ford acceptance company, etc., into almost subprime themselves?

● (1000)

Prof. Ian Lee: It may. It really depends on whether you, the parliamentarians, regulate the shadow banking. Right now they're not regulated, so they are not subject to the reserve requirements. Therefore, they can be more leveraged and make higher profits in good times—but then we saw what happens in bad times. If they were under the same or a similar regulatory regime, that may be problematic.

Hon. John McKay: I buy your basic argument that the shadow banking system is largely a no-man's land as far as regulation is concerned. I buy your basic argument that the banks have moved in. Lending is up in the banking sector, in part because the non-banking sector has abandoned the field. But the irony of the whole thing is that the cost of credit is going up for a lot of people.

Prof. Ian Lee: That's only because they're recapitalizing because of this extraordinary financial crisis. The losses are going to continue to rise. I was in the bank in the 1980-81 recession when Volcker was the chair of the Federal Reserve Bank, when people were losing their houses because they had a 10% mortgage and they were rolling up on the renewal at 18% and 19%. That's why I went back to university. I've said this to my students. I got tired of throwing middle-class people out of their homes and I thought there had to be a better way to make money.

Hon. John McKay: Don't you wish you'd bought bonds when they were 18%, 19%?

The Chair: Thank you.

Monsieur Carrier.

[*Translation*]

Mr. Robert Carrier (Alfred-Pellan, BQ): My first question will be for Mr. Serré, of the Canada Mortgage and Housing Corporation. The government's $2 billion action plan is rather interesting, except that there is no specific amount for two- or three- bedroom social housing. This is a specific request; there is a major shortage in this type of housing, at least in our ridings. Four hundred million dollars over two years is allocated to low-income seniors, but for families that need a two- or three-bedroom home, there's nothing specific.

We consider this to be a significant shortcoming within the stimulus plan. Obviously, you did not draw up the action plan, but I was wondering whether, at the very least, because you do represent government in the housing field, you had been consulted on the action plan. Were two or three bedroom homes a priority that you would have mentioned to the government?

Mr. Pierre Serré: Unfortunately, neither affordable housing nor social housing fall within my area of expertise. I am unable to answer your question.

Mr. Robert Carrier: However, those issues fall within your mandate. The CMHC deals with housing in Canada, and is well aware of the country's housing priorities. Therefore, I do not understand why this is not your area of expertise.

Mr. Pierre Serré: I deal with mortgage loans and insurance. I was not clear, I apologize. I am the vice-president responsible for mortgage insurance, and I'm not responsible for either affordable housing or social housing. I do not have the knowledge necessary to answer your question.

Mr. Robert Carrier: Your area is rather limited.

Mr. Pierre Serré: It is well defined.

Mr. Robert Carrier: I have various questions concerning your organization. The government is obliging you to purchase risky mortgages. You have a budget, that is granted by the government, for the Insured Mortgage Purchase Program. This program is managed by the Canada Mortgage and Housing Corporation. Therefore, you have been given a new responsibility.

Would you be able to reply to a question on this subject? I am concerned about whether you have calculated a rate of return on these new purchases. Given that this is a mortgage purchase program, the risks are certainly quite high. Under the mandate that you have been given by the government, is there a fall-back provision for mortgages that are not honoured?

● (1005)

Mr. Pierre Serré: With respect to provisions concerning mortgages that default, all of the risk is being carried by the insurers. Mortgage insurers cover risk in the case of payment default. The Insured Mortgage Purchase Program run by the CMHC is not forecasting any losses due to default on mortgages. This is entirely covered by the insurers.

Mr. Robert Carrier: But the CMHC is the insurer.

Mr. Pierre Serré: It is either the CMHC or private insurers that are operating in Canada.

Mr. Robert Carrier: If the insurer assumes all of the risks, what is the use of the Canada Mortgage and Housing Corporation buying up mortgages, if there is no inherent risk?

Mr. Pierre Serré: The key is access to credit. It's essentially a way to increase liquidity for Canadian lenders, so that consumers, Canadians, can access credit, mainly for mortgages.

Mr. Robert Carrier: All right.

[*English*]

The Chair: One minute.

[*Translation*]

Mr. Robert Carrier: According to information I received about your corporation, you have accumulated a surplus. According to these figures that I have, the surplus currently sits at $8 billion. Can you please confirm for me that indeed the surplus you have accumulated is of that order?

Mr. Pierre Serré: Today, I do not necessarily have all of the information on the cumulative surplus, but I can certainly say that for insured mortgages, we have capital reserves that meet the standards of the OSFI. This was mentioned previously. Our reserves amount to $4.3 billion to support insurance operations. Therefore, our surplus is actually above and beyond $4.3 billion.

Mr. Robert Carrier: Didn't the Auditor General say that $2 billion would be a sufficient surplus to maintain your operations?

[*English*]

The Chair: Just give us a brief response, please.

[*Translation*]

Mr. Pierre Serré: The CMHC's surplus already belongs to the Government of Canada. Each time the CMHC earns one dollar, the government, in its books, can write up one dollar in revenue. Therefore, that consideration is not taken into account.

[*English*]

The Chair: *Merci*.

Mr. Dechert.

Mr. Bob Dechert (Mississauga—Erindale, CPC): Thank you, Mr. Chair, and good morning, ladies and gentlemen.

I have a question for Mr. Rabbior. Mr. Rabbior, I was looking at the "Newcomers to Canada DayPlanner" that you've kindly provided to us, and I want to commend you on assisting new Canadians with becoming familiar with the financial system in Canada. I can only imagine how bewildering it must be for some newcomers to Canada. I wonder if you could tell us a bit about how new Canadians without credit histories obtain mortgages in Canada and if you are aware of any problems they might be facing in that regard.

After you've had a chance to respond, I'll also direct a question on this to Mr. Serré.

Mr. Gary Rabbior: I'm not terribly informed on that matter. I just know that a lot of the newcomers whom we are working with, and whom we've worked through various agencies to try to assist, struggle with all aspects of getting their financial house in order once they come here, getting their credentials assessed and so forth.

In many cases, they're also concerned about whom to trust for advice and guidance. What we're finding is that, in many cases, newcomers are turning more towards their communities, towards those in their ethnic groups, religious organizations, which in some cases is problematic, because they may be turning to people who, though trustworthy, lack the expertise to provide proper guidance.

I know that the banks are increasingly trying to set up departments within their institutions to deal with newcomers. We've been involved with Scotiabank and also with Royal Bank and others who are trying to attend better to the needs of newcomers.

But your point is well taken, and it's not confined to the mortgage and credit issue, but it bears on various aspects of financial planning here in Canada.

Mr. Bob Dechert: Thank you.

As I understand it, newcomers without long Canadian credit histories are often unable to get mortgage lending from traditional bank lenders and they often have to go to non-bank lenders. In the current situation, although their mortgages may be in good standing, because of the lack of liquidity in the non-bank lending environment, many of them may be facing situations where they are unable to renew their mortgages in the near future.

Mr. Serré, I wonder if you have any knowledge of that. If you do, what might you suggest we do about it?

● (1010)

Mr. Pierre Serré: I'm not the expert on newcomers to Canada, but I'm fairly certain we have done some research at CMHC.

In terms of timing, it's not right away, upon landing in our country, where they need to access mortgage financing. They will want to access mortgages probably three years or five years from when they come to Canada. By that time it is likely they will have established a Canadian credit history.

From an access perspective—at least I can speak from Canada Mortgage and Housing's perspective—for mortgage insurance, we would treat all Canadians the same. We take a look to see if they have an ability and willingness to pay and manage their debts. Should they not have a Canadian credit bureau history, we are quite okay in looking at credit bureaus from the land they come from. We are also quite flexible—prudently flexible—in terms of looking at other forms of evidence that supports their ability and willingness to repay their debt. There is some flexibility in our underwriting requirements, though I can only speak from a mortgage insurance perspective. But if you're a first-time homebuyer, you're likely to be in the high-ratio world of 80% or more.

Our policy is to try to treat everyone the same, and we try to make sure that different types of evidence of ability to manage your mortgage can be brought forward—not just an employment letter, for example.

Mr. Bob Dechert: Would you say there's more that can be done to assist new Canadians in obtaining these CMHC-insured mortgages?

Mr. Pierre Serré: One of the important things would be to make sure there's more information in those communities—and I think that was just mentioned.

One of the things we're embarking on is translating. We have a number of information booklets—on mortgage insurance, for accessing housing and buying your first home. We're in the process of translating that into another eight languages and placing those items in the community.

I think it's quite right that newcomers to Canada are looking to their community for support, so that type of information, in their own language, is going to be very helpful.

Mr. Bob Dechert: Thank you.

Ms. Bose, did you have a comment?

The Chair: Yes, she wanted to comment on that.

Mrs. Anu Bose: I want to comment, as a returning Canadian. I'm just speaking as an individual now.

I was gone for 20 years, and when I came back my impeccable credit history from Lloyds Bank—which is now Lloyds Bank of Westminster, as opposed to plain old Lloyds Bank—and the UBS, in Switzerland, was not going to be considered by banks here. So I think certain immigrants to this country will need portable credit histories.

I didn't have a community to go to, and in fact I would rather eschew that kind of credit.

The Chair: We're over time, Mr. Dechert. We'll have to move on. You might have another chance.

We'll go to Mr. Pacetti, please.

Mr. Massimo Pacetti (Saint-Léonard—Saint-Michel, Lib.): Thank you, Mr. Chair.

Thank you to the witnesses for appearing. This is an interesting subject.

I have a quick question for Mr. Robbior.

I think Mr. McKay alluded to this, in the sense that it's great that you put all this material together, but do you think any of the economists or bankers out there have received any of your material? If they can't get it right, I don't see how we can educate—and never mind new Canadians, but Canadians in general.

It's a big challenge when the experts don't know what's happening and they can't give us proper advice. Here we have Mr. Lee, who just indicated he doesn't invest in banks.

Where do we go from here? It's not a criticism, but I'm wondering whether you are educating the wrong people.

Mr. Gary Rabbior: When it comes to what experts need to know to manage high-level affairs, it is complicated and complex, but when you come down to handling basic economic and financial matters in your life, it isn't extraordinarily difficult. The problem is that we've never put much effort or priority into trying to empower Canadians with the knowledge and skills they need, at even the basic level. It's understandable that some of those in our financial institutions, and elsewhere—in our Parliament and whatever—don't have the background themselves, because we didn't give a priority to making sure this is one of the areas people have a level of competence in.

The resources and whatever are getting used. They're being used in the schools and by newcomers. There is an incredible demand and desire for material.

You have two problems. People don't trust the sources of financial information. You have to win their trust—

● (1015)

Mr. Massimo Pacetti: That's my point exactly. To go back, we trust doctors; we don't necessarily try to learn how to read an X-ray or try to write a prescription.

So are we doing the wrong thing in trying to educate people? Yes, you're right, we are downloading or offloading onto people the management of their own RRSPs, RESPs, mortgages, and these are all complex instruments. As the days follow, more and more complex instruments will come out, but in the end they're probably not worth anything.

So is it up to the professionals? If a doctor fails in surgery or fails in giving you a diagnosis there are repercussions. Here there don't seem to be any repercussions.

Mr. Gary Rabbior: To draw on your analogy, the doctor often has an ability to try to explain the situation or circumstance you're in and what might be the best medication for you to take. We have a problem here in that often the communication on financial matters from those who are selling financial products is not necessarily clear or understandable by the people to whom they're selling. We have requirements for disclosure that say if I mail you something in the mail, I've disclosed the information. It doesn't necessarily mean you've even seen it, let alone read and understood it.

Part of what we have is no obligation, no commitment to making sure that the Canadians who are desperately trying to make decisions and handle their affairs are being provided with both the capacity and the information and language to understand them. What we have developed as an expertise in being able to explain some of these complex matters in clear language that people can understand.... Unfortunately, so much of the material from the private sector, governments, and institutions is very complex.

Mr. Massimo Pacetti: I know Mr. Arnold and Ms. Bose are both nodding their heads, but I want Mr. Lee to answer. How do we regulate the shadow banking system? You're asking us to regulate it, but it's a huge market. Where do we start and where do we end? What does it include?

Prof. Ian Lee: It's certainly going to include investment banks. It's certainly going to include hedge funds, the regulation of credit swaps, derivatives. There are all kinds of proposals being put forward in the States and in England. I think they're going to end up looking more like banks. We're not going to go back to the old days of the 1980s or 1990s after this crisis is over. I think the banks are going to return to the centre as the dominant financial institutions in both Canada and the United States, because the commercial banks—

Mr. Massimo Pacetti: The little guy is always going to need to borrow money somewhere. If the average bank won't lend him money he'll find it somewhere. If he has to he'll go to a Shylock. These are the kinds of things we have to prevent.

Prof. Ian Lee: I guess I don't really see that as a problem, and I'll explain why. There hasn't been a lack of access to consumer credit. Unfortunately, I didn't put the slide in showing the indebtedness of consumers in Canada and the United States. They are wildly overleveraged. The problem isn't being able to get credit at the consumer side; it's that they have too much credit in terms of what they can carry.

The Chair: Very quickly, please.

Mr. Massimo Pacetti: We have time. Go ahead.

[*Translation*]

Mr. Michel Arnold: As regards those who advise us on complex financial products, last year, Option consommateurs carried out an investigation on financial advisers in Quebec. According to this inquiry, half of all financial advisers do not request basic information to advise a consumer. For example, one is not even asked if he or she has children or is separated. I think this sector needs to be regulated.

[*English*]

The Chair: *Merci*.

Mr. Wallace.

Mr. Mike Wallace (Burlington, CPC): I want to thank the guests today.

I'd be highly shocked if Mr. Lee has RRSPs that don't have any bank stocks in them at all.

I'll start with Mr. Lee. I appreciate your presentation today; it was very good. Following up a little bit on what Massimo was saying on the regulation of the secondary lending market, do you think the consumer of these products actually understands that these lenders are not under the same financial regulation as the banks? Do you think there's a role for us to have the consumers understand who they're borrowing from and what the risks are?

● (1020)

Prof. Ian Lee: Certainly, I've always advocated transparency. To use the technical jargon, financial markets are more efficient when there is more disclosure of information because consumers can then make informed choices.

In terms of vehicles, such as structured investment vehicles and derivatives, the people buying these products are not “ordinary” consumers. For most consumers, average Canadians deal with a credit union, a bank, or a credit card, but do not deal with a structured investment vehicle. They're certainly not buying credit swaps, which is a different market. Some sophisticated investors were getting around the regulators and regulations by going outside them, because they could run up the leverage ratios and make more money, but it then blew back into the regulated financial system.

Mr. Mike Wallace: You're saying that, in your opinion, they understood the risks they were taking.

Prof. Ian Lee: No, I don't think so. I'm sorry. There is in fact a real criticism of how some wealthy people in the U.S. took everybody for a ride. But most of the CEOs with these huge bonuses have lost money because they thought the system was going to keep on going.

Mr. Mike Wallace: Okay. I appreciate that.

I'm going to ask the same question in English that was asked in French, to make sure everybody understands. I'm going to go to Mr. Serré. In the current budget that has recently been passed, there is a facility for CMHC to buy mortgages that are insured. To be clear, and for the public's edification, you're buying mortgages that banks have offered to people. They lent them the money. Those mortgages are insured. They are covered by an insurance program. They bundled them together. For the banks to have more money or to have money to actually lend, you're buying the bundles and giving them cash for those bundles. Is that an accurate way of putting it?

Mr. Pierre Serré: Yes, that's accurate.

Mr. Mike Wallace: The money that the banks get should then in turn ease the credit crunch, as they call it, to allow them to again lend that money to somebody else who is creditworthy. Is that correct?

Mr. Pierre Serré: Absolutely, that's the intent.

Mr. Mike Wallace: Thank you very much.

I have another question on a different line. I have a summary of the recent corporate plan for your organization. On one of the lines it says more than one-third of CMHC's business is in markets that private mortgage insurers do not serve or that are less active, including low-cost mortgage financing. You take some risks in some areas, I would say, where others don't take risks. Do you have a competitive advantage over the private sector because you're a crown corporation?

Mr. Pierre Serré: As a crown corporation, we have a mandate to be everywhere in Canada. We have a mandate to offer all the products to all Canadians across the country. We also do rental housing. That is our mandate.

Mortgage insurers in the private sector do not have that requirement imposed on them by OSFI, which would regulate them. We are required to have a reasonable rate of return on a level playing field in a competitive marketplace. The expectations of CMHC are slightly different from that of the private mortgage insurers in that we have a mandate to serve all Canadians everywhere. As I mentioned in my opening statement, it includes rental housing, nursing and retirement homes, chattel homes, which are mobile homes up in the north, single industry towns, and rural areas. We are everywhere.

The Chair: Mr. Wallace, you have about 15 seconds left.

Mr. Mike Wallace: Thank you very much.

I only want to say one thing to the folks from the Canadian Foundation for Economic Education. That was excellent material. I'm hoping to call them to come to Burlington to give a presentation to the public.

Thank you very much.

The Chair: Thank you.

I believe Ms. Bose wanted to briefly comment on your first question.

Mrs. Anu Bose: I only wanted to say that when we had our seminar or colloquium in Montreal, Ira Rheingold, who was one of the speakers, said credit is a product that is sold to consumers and it is not a contract between the parties. Disclosure is therefore no substitute for clarity and caveats.

Thank you.

The Chair: Thank you.

We'll go to Mr. Pacetti again.

Mr. Massimo Pacetti: Thank you, Mr. Chair.

Mr. Serré, were you saying that the private sector insurers are not regulated?

● (1025)

Mr. Pierre Serré: Yes, they are regulated. The private mortgage insurers are regulated by the Office of the Superintendent of Financial Institutions.

Mr. Massimo Pacetti: Can we just go over the amount you seem to be picking up in mortgages? It says here that in 2008, $43.5 billion of CMBs were issued, and then you have the $61 billion of NHA mortgage-backed securities, and now you're going to have another $125 billion? As you just responded to Mr. Wallace, you're trading mortgages for cash, so you no longer have cash? Is that it? How much of those mortgages that you're buying pose a risk for you? I guess ultimately that would be the question. What is the difference between now and last year,let's say? All of a sudden the government is giving you an extra $125 billion to spend, which you didn't have before?

Mr. Pierre Serré: We've had the Canada mortgage bond program since 2001. It issues securities to the public—large and small investors. That money goes to the banks for them to lend more money. In terms of the insured mortgage purchase program, the recent program was introduced late last fall. We borrow money from the government and in turn buy the mortgages from the lenders.

Mr. Massimo Pacetti: And then the $125 billion will work in the same fashion? Is that correct?

Mr. Pierre Serré: Yes, to date—

Mr. Massimo Pacetti: So you won't have any cash. You'll have $125 billion of mortgages?

Mr. Pierre Serré: In the first instance, we did not have cash necessarily. We borrowed from the government. They provide the cash, and then that cash is flowed to the lenders in return for the mortgages that we would be purchasing on behalf of CMHC.

Mr. Massimo Pacetti: How much of that would be at risk if the real estate market were to decline by, say, 10%? Would you be at a 10% exposure rate or would you be at a bit higher rate? Are we looking at another Fannie Mae and Freddie Mac?

Mr. Pierre Serré: Now that gets into the other side of the house, which is my side—the mortgage and insurance side of the house as opposed to the securitization side, which is where all these programs exist. All of these mortgages are already insured. As I said before, if we rerun our mortgage insurance program, just as any private insurer would, we price for the long term. Pricing for the long term means that our price includes provisions for economic downturns like the one we're experiencing now, the one we experienced in 1990, and so forth. So we are adequately provided for from a reserve perspective. We follow the Office of the Superintendent of Financial Institutions' capital rules. We have a target of 150% of their minimum, and we're actually well above 200%. So we are very well positioned to weather these economic storms. And the key drivers from our perspective—although you are quite right that house price declines are a driver—would be jobs. Unemployment rates would be a key driver.

Mr. Massimo Pacetti: You mean the person's ability to pay. So even if the prices went down, if the person kept paying his mortgage, it wouldn't really bother you?

Mr. Pierre Serré: Interest rates are low right now, and they're stable—

Mr. Massimo Pacetti: But my first question was if you're getting an extra $125 billion, and you're lending out that whole $125 billion, where's the reserve on that $125 billion? Shouldn't you be taking a 10% or 15% or 20% reserve on that additional...?

Mr. Pierre Serré: Those mortgages are insured, as I said, so to the extent that there are any reserves, they're maintained by the private mortgage insurers and not as a result of the IMPP program. They are as a result of the mortgage insurance program. For that, OSFI requires you to have fairly large reserves for the insurance you have written.

Mr. Massimo Pacetti: My next question is whether the $125 billion you're using to purchase mortgages is being used to purchase good-quality mortgages or just to purchase mortgages that the banks don't want.

Mr. Pierre Serré: We are purchasing only high-quality assets. The reason they are high-quality assets is that they're already insured, and that insurance is backed by the federal government.

Mr. Massimo Pacetti: How do you determine that they're insured? How do we know they're not the same type of instrument as the asset-backed securities, which were just a whole bunch of stuff put in baskets? Do you actually go through each list and say, “Okay, Mike Wallace's mortgage—very good”?

Hon. John McKay: It's high-risk.

Voices: Oh, oh!

Mr. Massimo Pacetti: He admitted to it last week. I would actually lend him a lot of money.

The Chair: Could we have just a brief response?

Mr. Pierre Serré: I can't comment on any individual's mortgage. However, the program is such that it insures that every single mortgage that is purchased is insured by either the Canada Mortgage and Housing Corporation or the other two private mortgage insurers. So there are processes in place to ensure that uninsured mortgages do not enter the program.

● (1030)

Mr. Massimo Pacetti: Thank you.

The Chair: Thank you. I'll just remind the vice-chair that we can always set up a subcommittee to discuss Mr. Wallace's financial predicament.

We'll go now to Mr. Del Mastro, please.

Mr. Dean Del Mastro (Peterborough, CPC): Thank you, Mr. Chair.

Mr. Lee, I have a couple of questions for you. To begin with, you talked about the NINJA mortgages. I did a bunch of looking into that and, without going too far with this, what really bothered me with the NINJA mortgage wasn't just that they existed in the first place; it's how they mutated and came out the other side as prime paper, so we had the mutant NINJA mortgages.

Somebody is ultimately responsible for that, are they not? Isn't this a failure of the bond rating services and so forth that actually looked into this? It's not just that there wasn't regulation; it's that there wasn't regulation and that the groups that would actually evaluate this totally missed it, didn't they?

Prof. Ian Lee: I didn't mean to lay it all on the Congress. What I meant was, that was where it started because they are the referees. They have to set the regulatory framework. However, Fannie and Freddie then made some absolutely colossal errors. They are bankrupt; they were bought and nationalized. And then the bond rating agencies failed to rate them properly.

So there were failures throughout the mortgage creation value chain, if I can use a technical term. I don't absolve them. I think there are very serious problems in the whole credit rating...and I'm referring now not to the banks that are evaluating the individual mortgage, but to the bond rating companies that evaluate. There's no due diligence there right now, or, I should say, there's no oversight.

Mr. Dean Del Mastro: I agree. Let me actually go one more step on that before I change topics. Your graph showed the demand for housing, the price for housing, ramping up very, very rapidly. There have been an awful lot of economists who have come forward and said, listen, there will be no economic recovery in the United States until they stabilize the banks first and then the real estate market.

There must be a bottom in the real estate market. Where's the bottom in the U.S. real estate market? Does anybody know that? Are we there? Are we getting there?

Prof. Ian Lee: I have seen a couple of very good estimates and they are wildly different. They're from two very respected people: Don Drummond, in a presentation he gave last week from TD Bank, estimates that they're about 10% away from the bottom. However, the analysis from Schilling in the States, who is a well-known mortgage and realty economist, estimates there's another 20% decline, so it's somewhere between a 10% and 20% decline. He's predicting a 37% decline on average across the United States from peak to trough. These are staggering numbers.

Mr. Dean Del Mastro: So I would expect that where we really saw the huge fluctuations, it was regional, and that you could see properties at half or even lower value—

Prof. Ian Lee: Indeed. I have many more slides. I have a map of the United States showing the degrees of foreclosures and failures. The two coasts of the United States have overwhelmingly received the worst. They have been affected the worst. The inland or the heartland, or the states in the interior, had a much more modest housing bubble and a much more modest decline. Therefore, they had much more modest losses.

Mr. Dean Del Mastro: Okay.

The Chair: You have about a minute and a half.

Mr. Dean Del Mastro: Thank you.

A single securities regulator.... I can't for the life of me understand why any region in the country wouldn't want to move towards a better system of securities regulation. What message would you give to those areas that are actually pushing back and saying no, this is a provincial jurisdiction? This is really about protecting consumers. It's really about protecting Canadians.

I think the potential is there for our financial system to move ahead and buy assets at a bargain price and really step forward and make Canada a financial leader with a huge financial industry, much bigger than what it was going in. However, we've got to get this single securities regulator in place. What would you say to those areas that are pushing back on this? I don't understand it myself.

Prof. Ian Lee: I should have said this in my earlier response. I believe it's in the self-interest of every region. It's in the self-interest of every Canadian that we have a single national regulator because it will insure much greater safety of financial investments and financial securities. That will minimize or mitigate the potential losses to people whether they're living in Alberta, Quebec, or Ontario, and it will enhance our competitive advantage. I do not understand any argument against a single securities regulator, and I've looked at this for a long time.

● (1035)

The Chair: We will go to Mr. McKay.

Hon. John McKay: Thank you, Mr. Chair.

Professor Lee, in the business papers there has been a bit of a food fight going on between the Bank of Canada and OSFI about regulatory supervision of financial institutions. You're sort of staying on the sidelines watching this.

On the one hand, we seem to have a fairly well-regulated institutional structure, where everybody seems to be at the table. On the other hand, the Bank of Canada seems to want to step in and take supervisory jurisdiction. It appears that the bank may have committed us in international circles to go in that direction.

What are the pros and cons here? What is the net gain or benefit for Canada if in fact we go in that direction?

Prof. Ian Lee: That's an excellent question. It's been debated, of course, in the States as part of their examination of reregulation. Currently the U.S. is the only system where the central bank regulates the banks—inspects, audits, regulates the banks. The other major countries in the world do not. They've divorced it from the central banking system.

There are arguments for and against. The argument is that the central bank has a deeper understanding of the macroeconomy and monetary policy and monetary conditions than anybody else. The counter-argument is that they are in a conflict of interest in terms of their mission, somewhat similar to CMHC; they have a conflict between their commitment to social housing, which is very legitimate, and their commitment to being a mortgage insurance company.

The central bank, if it becomes the regulator of banks, is in a conflict because its primary job is to ensure stability of the financial system, integrity of the currency, and moderate price inflation. And yet, if they're responsible for banks and they have to bail out a bank from time to time, they want to do things on the monetary policy side to help that particular bank.

So I'm also sitting on the fence, because I've seen very good arguments on both sides. But the preponderance of the evidence is that in the G-7, only one country at the moment has given the regulatory authority over banks to the central bank, and that's the United States.

Hon. John McKay: It didn't seem to work for them, did it?

Prof. Ian Lee: And it didn't seem to work for them.

Hon. John McKay: The other area that you talked about in previous testimony had to do with the non-banking sector, which is 50% of the market. When you're talking about the non-banking sector, are you including in there provincially regulated institutions? Are you including pension plans, things of that nature? They're huge players in the marketplace, and yet it seems that most of our difficulties in this country come from that sector.

Prof. Ian Lee: I was hoping, actually, that I wasn't going to be asked that question.

Voices: Oh, oh!

Prof. Ian Lee: I didn't want people from different provinces to be shooting at me.

We've learned in the last five, six, seven years—Volcker has said this, David Dodge has said this, others have said this—that all financial markets are interconnected. They are deeply interconnected because of the nature of financial markets. They are fungible. They are virtual. They are not physical. Money is mobile, instantly mobile.

For that reason, I think the distinctions between federal and provincial in terms of financial markets are completely artificial. When I was in the bank, we dealt with credit unions all the time, and yet they were under a completely different regulatory regime.

Take pension funds; I'm at Carleton University, and our pension fund is regulated by the Province of Ontario. I'm in Ottawa, where many of the other pension funds are regulated federally. Yet they're in the same markets. They're investing in the same package of securities. They're on the same TSX.

I think it's inevitable that we'll have to confront the day when all financial organizations come under a single regulator. This includes credit unions and pension funds. I do understand, though, that it would be very unpopular.

Hon. John McKay: Yes. We have political sensitivities around here that make absolutely no sense at times. But that's another issue.

Voices: Oh, oh!

Hon. John McKay: Greater scrutiny of CMHC is in the risk profile. In another life, I used to be a mortgage lawyer—doing mortgage remedy work, which made me very popular. What I don't quite understand in CMHC is that initially they insured the package of loans. Now they are in effect borrowing money from the government to buy the loans that they've already insured, effectively shifting the risk to the taxpayer.

Is that where we're at?

● (1040)

Prof. Ian Lee: No, I would respectfully disagree with you. The Government of Canada had already taken on the risk the moment they insured the mortgage. All they've done is taken over the physical title to the mortgage, if you will. The bank has conveyed the mortgage. It is as if I sell my car to you. You pay me cash, I give you my car; you get the car, I get the cash. That is what the government has done with the chartered banks.

That money, whatever it is, the $75 billion or $125 billion, has gone into the banks so they can reinvest, re-lend in the mortgage markets and in the credit markets.

The Chair: Mr. Serré, do you have anything to add to that? Okay.

Mr. Carrier.

[*Translation*]

Mr. Robert Carrier: Thank you, Mr. Chair.

I wish to remind my colleague Mr. McKay that the sensitivities he was referring to earlier are also called areas of jurisdiction. In our country, there are federal and provincial areas of jurisdiction. It is important to be reminded of this if we want to avoid continuous problems involving the interpretation of areas of jurisdiction.

I have a question for Mr. Rabbior, who represents the Canadian Foundation for Economic Education. You have graciously provided us with very interesting documents. Who funds your organization? Perhaps you already mentioned this, but I did not hear the answer.

[*English*]

Mr. Gary Rabbior: We don't get any sustaining funds at all. We're actually project funded. It makes us be what we teach, and that is entrepreneurial. We have to identify needs, we have to come up with ideas, and we have to find people who are willing to fund them. So we get funding from the federal government, provincial governments, the corporations, foundations, and some industry association partners.

[*Translation*]

Mr. Robert Carrier: Thank you.

You have a great document that is targeted to newcomers, and this document is partly funded by the Department of Citizenship and Immigration. Is the document distributed by the identified partners to all new immigrants who arrive in Canada?

[*English*]

Mr. Gary Rabbior: It is funded by HRSDC. We distribute it through over 600 immigrant-serving agencies across Canada. We provide it free to them, they order it, and they put it into the hands of newcomers.

Both HRSDC and CIC help us with connecting with newcomers, but primarily the distribution and connection that we have is through the 600 immigrant-serving agencies that work directly with them.

[*Translation*]

Mr. Robert Carrier: That's fine.

The document concerning young people and money is very interesting. I noted that there is very little involvement of Quebec representatives. It is surely because of the issue of sensitivities, as referred to earlier, and the fact that education falls within provincial jurisdiction. Is this the case? Is this document distributed in Quebec schools, since it does target young people?

[*English*]

Mr. Gary Rabbior: I don't think much has been mentioned of any particular province. So it hasn't been provincialized in that degree. It is distributed through the schools and also to individuals who want to use it with their children or grandchildren.

Jean Lapierre mentioned this book on the air about five years ago. We had 60,000 phone calls in two and a half weeks. That comes back to my point that there is a hunger and a demand for this kind of information. What happened there is that someone who was a trusted source said this book isn't trying to sell you anything, it's something you should get for your kids, and the doors opened.

I think what it is, is we need to have more trusted sources that Canadians can go to knowing they're not being sold a product. This is one effort on our part to try to provide that, particularly to young people.

[*Translation*]

Mr. Robert Carrier: Did you say that the document is distributed in Quebec schools?

[*English*]

Mr. Gary Rabbior: Any teacher can order a class set for free.

[*Translation*]

Mr. Robert Carrier: Is there already an agreement?

[*English*]

Mr. Gary Rabbior: I could provide you with a list of schools that order it. It is not distributed generally. It is only on request, when a teacher wants it. Our cost of the resource is a one-page evaluation. The teacher has to tell us what they think of it and how they're going to use it, and in return for that they get free copies for their students.

● (1045)

The Chair: Okay. In a minute.

[*Translation*]

Mr. Robert Carrier: I have another question for the representative from Option consommateurs. You did not submit any written document. Is there one?

Mrs. Anu Bose: Yes. We sent it.

Mr. Robert Carrier: I did not receive it, and was unable to retain your recommendations, which are surely important. I would therefore like to receive a written copy.

Perhaps the following was not in your recommendations, but do you feel that the Canada Mortgage and Housing Corporation is fulfilling its role as a guarantor, with respect to consumers? In the past, it has been a very significant reference.

[*English*]

The Chair: Okay.

[*Translation*]

Mr. Michel Arnold: I believe that the Canada Mortgage and Housing Corporation is playing its role. Of course, the various roles played by the various crown corporations can always be improved. Our second recommendation is very significant with respect to accountability mechanisms that financial institutions need to build in to their own lending accountability criteria when assessing a borrower's ability to pay back credit.

If you will, Mr. Chair, I will mention briefly that in January, 14,024 Canadian families were unable to make a mortgage payment. This represents an increase of 29% relative to October. Therefore, 3,158 families were unable to pay back their mortgage loan.

The Chair: Thank you.

Mr. Robert Carrier: We were told that the written document was sent. Did we receive it?

Mrs. Anu Bose: Our statement was sent to your office this morning, but you were not there.

Mr. Robert Carrier: Is it possible to obtain a copy?

[*English*]

The Chair: We said this morning, so we will get it translated.

Mr. Rabbior, can you e-mail the clerk explaining the contact information for your organization in order to get copies of those books so that the members can forward them to the schools? I know there are certain groups like the Mennonite Centre for Newcomers in Edmonton that would appreciate these documents. If we can get that sent to the clerk, we will distribute it to all members of the committee.

Mr. Gary Rabbior: I brought a handout, but unfortunately the French version is out of print right now. It has my business card and whatever on it; it is a resource too. I will certainly provide that to the clerk.

The Chair: Thank you.

We will go to Mr. Wallace, please.

Mr. Mike Wallace: Thank you, Mr. Chair.

I have just a couple of quick questions.

I think it was this past week that the banking institutions indicated that they're not as in need of support as they thought. Their credit seems to be easing up.

Does that affect the auction? Does that affect the bundling of mortgages and the availability of CMHC to buy bundles of mortgages from them? Has that slowed down? Do you think we'll use up all the $125 billion or whatever is in the kitty?

Mr. Mark Chamie (Treasurer, Canada Mortgage and Housing Corporation): You're quite right. In the last couple of auctions we've seen it hasn't been 100% full take-up on the auction. I think it was fully expected at the outset of this program that sometimes we'd see full take-up of the auction and at other times we wouldn't. It really depends on the needs of each financial institution and the level to which they want to participate. That is very dependent on each individual situation at that particular time.

What we've committed to is to deliver this program that the government has put forward in which we will purchase up to $125 billion of these NHA mortgage-backed securities. By doing that we'll offer regular auctions in which they can sell those NHA MBSs to us.

Mr. Mike Wallace: I appreciate that clarification.

Mr. Lee, thank you for your comments about the securities regulator, that it is voluntary and that provinces can opt in and out if they want. Let's hope they will all opt in when it actually happens.

You talked about leasing and banking and automotive. I happen to be sitting in on a subcommittee on the automotive industry for the industry committee, and there's one individual who keeps blaming the banks a little bit for the automotive business being in trouble. But the banks are not in the leasing business; they're in the business of loaning money on car loans, and they would be evaluating those car loans based on the credit risk of the individual asking for them. Is that not correct?

● (1050)

Prof. Ian Lee: In fact, I did that. It was called a floor plan or a dealer plan, where the bank would go in and finance the entire dealership on the business side. We would provide the loans to the business, because every car on that lot and every dealer in Canada is financed by a bank somewhere.

Then they would feed the individual deals to us in the bank and we would approve them on a one-by-one basis if we were floor-planning that dealership.

Mr. Mike Wallace: There's a facility offered through this budget that's been passed for $12 billion. Basically, the car manufacturers and the dealers are saying that 40% or 50% of their business used to be leasing. It depends on which company you talk to, but it's gone to near zero.

That $12 billion is really for those leasing arms of those manufacturers to be able to move, as they like to say on the commercial, iron or steel off their lots—actually, to move cars. It's not a bailout. It's not an option for the bank to gather this money for leasing purposes.

Would you agree with that statement?

Prof. Ian Lee: Yes, because the banks are prohibited from leasing directly.

Mr. Mike Wallace: And that's in the Bank Act?

Prof. Ian Lee: It certainly is.

I'm not saying it would solve their problems, but it would certainly alleviate their problems if some additional capital was provided to leasing by allowing the banks to come in. The acceptance companies can't because they're broke.

Mr. Mike Wallace: Right, and even if the banks were in the leasing business, do you think there would be an opportunity for them to be competitive? They would compete on interest rates because they're interested in making money on the financial product of a lease, not on moving a car off a lot. Is that correct?

Prof. Ian Lee: I realize this is speculative. I don't have data, and I'm a very data-driven kind of person. But we have never tested this. I think you will see, if it was approved, that the acceptance companies would be working side by side with the banks. Some will go through the acceptance company: the Honda acceptance company, GMAC, and so forth. Some will go through the bank. Some like going with banks; some like dealing with acceptance companies. It's about consumer choice in the marketplace.

Mr. Mike Wallace: Thank you very much.

The Chair: Thank you.

We'll go to Mr. Pacetti.

Mr. Massimo Pacetti: Thank you, Mr. Chair.

I have some quick questions, Mr. Serré. Are you also buying mortgages from credit unions?

Mr. Mark Chamie: Yes, we'll purchase an NHA MBS from any approved NHA MBS issuer, which includes credit unions.

Mr. Massimo Pacetti: The second question is just to go around this insuring and then buying back. So the CMHC or the government would secure a mortgage with a bank that a bank holds or has issued, and then you would buy it back within this $125 billion program or in some of the other programs.

Is all this being done free of charge? Who is making the money? Initially, you're charging a fee for the insurance, so CMHC is making the money. The bank makes the money on the spread.

Mr. Pierre Serré: I'll talk about the mortgage insurance side again and Mark can take over and talk a bit about the IMPP process.

From the mortgage insurance perspective, we charge a premium on all mortgages whether they're sold into the IMPP program or not, as do the private mortgage insurers. So there is a fee, an insurance premium, for that default insurance.

Mr. Massimo Pacetti: That's what the consumer pays. He pays that separately. It's not included in the mortgage price. Correct?

Mr. Pierre Serré: Normally, in Canada, the practice is that the borrower will pay the mortgage premium and it is put on to the balance of the mortgage.

Mr. Massimo Pacetti: Okay. So now the bank will sell you back this mortgage and that will represent the fee? Who will make money on that? Is that a discount or is that a premium?

Mr. Mark Chamie: Well, no. When we purchase the mortgages through this insured mortgage purchase program in the form of NHA mortgage-backed securities, we hold auction processes. So these financial institutions are telling us at what rates they are willing to sell us these MBSs, and hence, for the government, we purchase the MBSs that offer the highest yield and work our way down until the entire auction has been sold.

The government itself, though, sets a minimum rate at which it is willing to buy these NHA MBSs, and this rate is at a—

● (1055)

Mr. Massimo Pacetti: But aren't they matched? You're not buying something that is being lent out at 6% for 10%.

If you're saying, I want to buy only securities that lend out at 10%, but it's actually paying 6% because that's what the bank lent out at.... That's not what's happening?

Mr. Mark Chamie: No, that's not what's happening.

Just by way of the structure of the NHA MBSs and the prices at which they must sell them to us, the interest rates have to be within a certain band and—

Mr. Massimo Pacetti: What is that band?

Mr. Mark Chamie: Well, again, it depends on what the actual interest rates are in the marketplace and what NHA MBSs are selling for.

So the price of the NHA MBSs we are looking to purchase is somewhere around par level, but in essence, the yields at which we purchase the NHA MBSs are passed on to the government. As the Department of Finance said at the beginning, these will yield rates higher than their own borrowing costs.

Mr. Massimo Pacetti: Okay. So you're making money on this. Is the bank losing money on this?

Mr. Mark Chamie: No. CMHC is passing on the yield at which it purchases it to the government. As the government says, this yield is at a rate that is higher than their own borrowing costs.

Mr. Massimo Pacetti: Okay. But is the bank making money on them because they're transferring the mortgage more or less at cost?

Mr. Mark Chamie: No. They maintain a spread for the servicing of the mortgages, but the yield in which they're selling it to us at then becomes their cost of funds, and they would not look to make a loss on that.

Mr. Massimo Pacetti: They would not look to make a loss and you are not looking to make a loss.

Mr. Mark Chamie: While CMHC does not make a profit or a loss on this, the yields in which we purchase them at are passed on to the government.

The Chair: Thank you.

I just want to follow up very quickly on two points. One is the issue that Mr. Dechert raised about the alternative mortgage market. The government has moved in with the insured mortgage purchase program to inject liquidity into that side of the market, but in terms of the other side of the market, is there anything you'd recommend or anything the government should be looking at in terms of the liquidity in the alternative mortgage market?

Mr. Serré.

Mr. Pierre Serré: I think I would be outside of my purview on that one because of the recommendation.

The Chair: Okay.

Mr. Lee, do you have a comment on that?

Prof. Ian Lee: Sorry. Can you repeat the question?

The Chair: In terms of the alternative mortgage market, Mr. Dechert raised the issue of someone moving to Canada who, not having a credit history in Canada, would not go through CMHC. They call this the alternative mortgage market. Is there something that could or should be done to improve liquidity in that market?

Prof. Ian Lee: Are you talking about new Canadians coming to Canada? Is that what you're referencing?

The Chair: It's new Canadians or it's—

Prof. Ian Lee: It's actually in the mortgage lending market. People may disagree with me, but let me give you an example. If you walk into a bank with a 25% down payment in cash, not borrowed, you're probably going to get the mortgage. Banks are in the risk management business. The more down payment, the less risk.

That's why I made the comments in my opening about zero down payments on mortgages. That's very, very high risk. Twenty-five percent down is low risk, and a new Canadian can get a mortgage.

The Chair: Let me come at this another way, then. What percent of the mortgage market in Canada is covered through CMHC?

Prof. Ian Lee: I don't have that figure at my fingertips. I've seen the figure, but....

Mr. Pierre Serré: Are you asking in terms of the securitization?

The Chair: Yes.

Prof. Ian Lee: Good question.

Mr. Mark Chamie: Total NHA MBSs outstanding and Canada mortgage bonds represent in the area of 22% of the mortgage market.

The Chair: What percent of the market would be covered by the alternative mortgage market, then? I'm told it's as high as 30% of the mortgages.

Hon. John McKay: Do you mean private mortgages?

The Chair: Yes. I guess we'll have to ask another group.

There's a second issue I wanted to just quickly follow up on.

Mr. Lee, you talked about a national securities regulator. I appreciate that, but do you have recommendations in terms of how you would regulate asset-backed securities, derivatives...? The securities regulator is certainly one model, but you then need to have a system of regulation that falls under that model.

Prof. Ian Lee: I haven't drilled down to that level yet, but there are proposals floating around in the States and in England. I can certainly get some ideas to you very quickly, but I don't have them with me.

● (1100)

The Chair: Okay. I would appreciate any information on that.

I want to thank all of you for being here with us today. If you have any further comments or any information you want to submit to the committee, please do so.

The meeting is adjourned.

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