



June 12, 2014

The Secretary
Ontario Securities Commission
20 Queen Street West
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Toronto, Ontario M5H 3S8

comments@osc.gov.on.ca

**Re: CSA Proposed Amendments Relating to the Offering Memorandum (“OM”)
Exemption**

On behalf of the Mortgage Brokers Association of BC (MBABC), I would like to make submissions on NI 45-106.

By way of background, the MBABC is a 25 year old professional association which represents mortgage brokers and many private mortgage lenders in British Columbia. We estimate that in BC, mortgage brokers fund an estimated \$15 billion dollars annually. Many of our members fund private mortgages through mortgage investment corporations and mortgage syndications. In addition, we also represent mortgage investment corporations (MICs), syndicators and other private mortgage lenders who operate primarily in BC.

We are interested in commenting on the OSC proposal even though this is not a current proposal of the BCSC, as we understand one of the goals of the provincial securities regulators is to harmonize regulatory requirements between provinces. In addition, we understand that the BC Ministry of Finance is currently drafting a new *Securities Act* which will create a joint cooperative securities regulator between BC and Ontario, and this new regulator will replace BCSC. We further understand that the head office of the new regulator will be in Toronto and it will administer a single set of regulations between Ontario and BC. It therefore appears that there is a high probability that the OSC proposal could impact the BC industries which are currently regulated by BCSC.

The OSC Proposal

There are two aspects to the proposal which are of concern to us, which are identified below.

1. \$30,000 Annual Investor Cap for OM Exempt Investments

Proposal: Individual investors that qualify as eligible investors (but do not meet the accredited investor definition), are capped at \$30,000 on the amount that can be invested under the exemption in a calendar year.

We have the following issues with this element of the proposal.

No Harmonization with BC

The rationale for the introduction of the OM exemption in Ontario is stated in the proposal as follows:

We are proposing the OM Prospectus Exemption because we think that it may support the capital raising needs of issuers that are moving beyond the early stages of development. In order to facilitate harmonization, we have based this exemption on the existing OM prospectus exemption in section 2.9(2) of NI 45-106, which is currently not available in Ontario. We have worked closely with staff of the Alberta Securities Commission, the Autorité des marchés financiers, the Financial and Consumer Services Commission (New Brunswick) and the Financial and Consumer Affairs Authority (Saskatchewan) in formulating the OM Prospectus Exemption.

In BC, as you are likely to be aware, there is currently no investment limit on the OM exemption. While the creation of an OM exemption with a \$30,000 investor cap in Ontario may facilitate the capital raising needs of a constricted Ontario exempt market, the same exemption in BC would cripple the exempt markets – perhaps even kill some of the industries, such as BC's MICs. This will result in investors losing a choice for a highly demanded product and capital markets will not work as efficiently as MICs play a vital role in capital raising that the banks do not fill.

When looking to harmonize the Ontario OM exemption with other provinces, why not examine the exemption that is currently in place in BC, instead of Alberta, Quebec, New Brunswick and Saskatchewan? Perhaps there is a reasonable explanation here. However, given the commitment between the provinces of Ontario and BC to share a common regulatory structure, would it not be appropriate to review the BC OM exemption requirements? The optics of failing to harmonize Ontario's proposed new OM requirements with those of BC in light of the single regulator plan are simply not good.

Satisfying Investor Protection Goals

It is not entirely clear what the specific goals are of the OM investor cap of \$30,000. The OSC proposal provides the following rationale for the cap: "In our view, limits on both eligible and non-eligible investors are appropriate to limit the amount of money that retail investors invest in the exempt market". Are the goals then to save investors from the folly of investing too much of their hard earned money in the exempt markets, or is it an effort to limit the harm to investors from investor frauds, such as ponzi schemes or sham investment entities?

As you may be aware, government regulation is usually ineffective at reducing fraud, as fraudsters never intend to comply with rules, particularly ones that would limit the funds they can misappropriate. Creating more rules or more restrictive rules will not change this

unfortunate reality. Tackling investor fraud will likely require a collaborative effort between criminal justice systems, government regulators and the industry.

Failing to Empower Consumers

The governing principal behind the exempt market is that investors take on risk. This is why they sign a risk acknowledgement form and receive suitability advice from a registered exempt market dealer. In addition, investors can read an OM which contains details of the investment, which is often more detailed than a prospectus. The OM contains protections for investors, including the right to sue directors for misrepresentation and the right of rescission. Taking away investor choice by placing low investor limits on OM exempt investments treats investors like children who cannot manage their own money and renders current investor protections redundant. We believe that consumers should ultimately be responsible for looking after their own interests and taking responsibility for their own choices. The goal of government should be to ensure that consumers are empowered to make informed, careful investment decisions. Providing consumers with relevant knowledge is actually a much more powerful consumer protection tool than imposing a system of paternalistic regulation over them.

Red Tape and Enforcement Challenges

The \$30,000 annual investor cap appears to be cumbersome to administer. It is not entirely clear how the investor's limits will be tracked? What if investor's are not honest in making investment declarations? Who takes action against the investor in this circumstance? What if the appropriate suitability advice rendered by an exempt market dealer is that the investor should invest more than \$30,000 in the exempt market? Does the exempt market dealer render that advice despite it being impossible for the investor to follow? The OSC might wish to choose whether to pursue investor protection using a client focused advisor model or a transaction based model containing a multitude of requirements and restrictions on investor transactions. The OSC should not attempt to implement a system containing mixed regulatory models with conflicting goals.

Impact on the Mortgage Investment Corporations and Mortgage Investment in BC

MICs contribute billions of dollars' worth of mortgage principal to borrowers in BC. Without MICs it would not be possible for many BC residents to afford to own their own homes, and many industries could not acquire the necessary capital for growth and development.

We recently canvassed some of the top MICs in BC, who reported that 54% of the funds they raised last year exceeded the \$30,000 per investor per year limit. A \$30,000 investment cap for BC MICs, at best, would result in the loss of over half of their principal, and a worst case and quite possible scenario is that BC MICs would be quickly eradicated due to a lack of financial viability. The impact on the mortgage borrowing public if the OSC proposal was adopted in BC would include:

- preventing some borrowers from completing mortgage transactions without the support of an added second or third private MIC mortgage;
- loss of employment from mortgage industry members and support staff who would no longer be arranging and administrating mortgages – also the loss of construction

- related employment from developers and builders who would not be able to finance developments;
- loss of safe and reliable investment opportunities for investors;
 - removing private mortgage lenders from the marketplace, which will make it more challenging for borrowers to find available mortgage capital but also push private lending underground where there is no regulation; and
 - higher borrowing costs and less access to mortgage capital will lead to an increase in foreclosure rates and borrower defaults.

2. EMD's related to the Issuer

Proposal: Registrants that are “related” to the issuer are prohibited from participating in an OM distribution due to significant investor protection concerns about the activities of some EMDs that distribute securities of “related” issuers.

The OSC might view independent EMD's as having fewer conflicts of interest than related party EMDs, as they appear to have no interest in the products which they sell to investors. However, independent EMD's are paid by commissions from the investments which they recommend investors to buy, and there is clearly an inherent conflict of interest here. Some EMD's might conceivably recommend investments based on the highest commission they earn and not based on what is the best product for the investor. This conflict may not be as apparent or as obvious as the conflict that MIC's have when they use a related EMD to sell their investments. However, hidden or less apparent conflicts can create higher risk to investors. The OSC has not acknowledged or otherwise addressed this serious concern in their proposal. In addition, to create a level playing field, the related party issuer model would have to be abolished for other sectors, like IIROC and the MFDA.

MICs in BC know their own product better than anyone else and are generally, the only parties who can competently advise investors of their products. Also, many MICs cannot afford to pay commissions to independent EMD's, which typically run upwards of 6%. Adding this cost to the capital raising process for MICs will make them uncompetitive in the private mortgage lending market, and render them unviable.

As a less draconian alternative to this proposal, the OSC might consider permitting issuers to distribute an exempt offering provided that comprehensive conflict of interest disclosure is provided to the investor.

For the reasons stated above, the MBABC recommends that the OSC:

1. not implement caps on the amount eligible investors can invest under an offering memorandum exemption to \$30,000 per calendar year; and
2. permit registrants that are “related” to the issuer to participate in an OM distribution provided that comprehensive conflict of interest disclosure is provided to the investor.

Thank you for the opportunity to make submissions on the OSC proposal. Please know that we are available should you have any questions concerning any of the issues discussed above.

Yours truly,

A handwritten signature in black ink, appearing to read "Samantha Gale".

Samantha Gale, CEO
Mortgage Brokers Association of BC

cc. BCSC, BC Ministry of Finance