

June 5, 2018

Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Financial and Consumer Services Commission (New Brunswick)
Manitoba Securities Commission
Nova Scotia Securities Commission
Nunavut Securities Office
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Ontario Securities Commission
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

**Proposed amendments to prospectus and registration exemptions
applicable to syndicated mortgage transactions**

About the CMBA

The CMBA is an inter-jurisdictional umbrella association consisting of provincial mortgage broker associations in Canada, including associations in Atlantic Canada (Nova Scotia, New Brunswick, Prince Edward Island and Newfoundland and Labrador), Ontario and British Columbia.

Nature of Proposal and CMBA Commentary

We appreciate the opportunity to comment on the CSA proposal, which contains a number of recommendations to amend available securities exemptions available to mortgage syndicators. The CSA proposal contemplates that the regulation of syndicated mortgages currently within the jurisdiction of mortgage broker regulators will transfer to or remain with securities regulators. The proposal therefore attempts to harmonize securities regulation relating to syndicated mortgages from province to province.

Syndicated mortgage originations are particularly strong in the provinces of Ontario and BC. The Financial Services Commission of Ontario (FSCO) reports that from 2016 Annual Information Return data, 105 mortgage brokerages in Ontario engaged in syndicated mortgage lending activity and funded \$6.6 billion in syndicated mortgages. Further, 36% percent of all syndicated mortgage activity is originated by entities which

are geared to syndicated mortgage lending on an exclusive basis, with the balance originated by brokerages in the course of their mortgage broker practice. This comment letter will therefore focus on syndicated mortgage practices in the provinces of Ontario and BC.

In addition, we are of the view that the CSA proposal contains some assumptions about the role of the licensed mortgage brokers who represent syndicated lenders and the structure of syndicate mortgage lending which are inaccurate and make the CSA proposal unworkable. We will therefore focus our comments on the challenges exempt market dealers would experience in taking over the role of dealing with syndicated mortgage investors from mortgage brokers.

The Ontario Case and BC Example of Regulation

In the 1990's there were no rules governing syndication mortgages in BC. However, legislative amendments to the BC Securities Act and Mortgage Brokers Act were introduced in 2000 after facts surrounding the mortgage brokering activities of Eron Mortgage Corporation (Eron) came to light. Eron was suspended by the Registrar of Mortgage Brokers in 1997, after it was found to have invested lender funds for syndicated mortgages without properly disclosing essential elements of the mortgage arrangements to the lenders. The new provisions divided syndicated mortgage activity into simple (qualified) syndications governed by the Mortgage Brokers Act and more complex (non-qualified) syndications governed by the Securities Act. The most significant consumer protection measure was the introduction of the lender disclosure form; it detailed essential information about the transaction and was to be provided by mortgage brokers to syndicated mortgage lenders prior to the release of funds to the borrower.

Now eighteen years later an Ontario case, very similar to Eron, appears to have become the impetus for regulatory change in that province. Already, the Mortgage Brokerages, Lenders and Administrators Act has been amended with new statutory changes resembling those in BC. They result in the division of syndicated mortgages into qualified (simpler) syndications and non-qualified (more complex) syndications, with different rules applying to each category. As of July 1, 2018, Ontario mortgage brokerages that deal with non-qualified syndicated mortgage transactions will be required to comply with stricter compliance measures.

However, the Ontario government has also recently adopted the objective of transferring regulatory oversight over syndicated mortgages from the mortgage broker regulator, FSCO, to the Ontario Securities Commission. This was Recommendation 17 of the expert panel report dated March 31, 2016 reviewing FSCO. Specifically, it recommended that "the government should require that documents issued to raise capital for syndicated mortgage investments be subject to the same level of regulation

as the securities regulator applies to other offering documents used to raise capital in the Province.”

The challenge is that Recommendation 17 has been made and adopted without a more in-depth analyses of how mortgages are actually syndicated and exactly who looks after the interests of syndicated investors. There appears to be an assumption that the role of licensed mortgage brokers under the mortgage broker regime dealing with syndicated investors can be readily swapped with registered exempt market dealers under the securities regime.

We note that the regulatory system in BC cannot be used as example of how syndicated mortgages can be regulated under the securities regime, as the vast majority of mortgage syndicators are exempt from market dealer registration. This is because they either arrange syndicated mortgages under the Mortgage Brokers Act or they rely on the current Mortgage Investment Entity Exemption (MIE Exemption) under BC Instrument 32-517.

How Syndicated Mortgages are Originated

Across Canada, syndicated mortgages are arranged by either mortgage brokers in the course of their general mortgage broker practice, or by specialized entities which engage in syndicated mortgage lending on an exclusive basis.

Many argue that recent syndicated mortgage failures under the spot light in Ontario were not actually examples of true syndicated mortgage lending and should not therefore be used as a basis for regulatory change. One of our members has explained that in these cases they “were able to dupe the public and the regulators by the simple action of registering a collateral charge on title (a mortgage) to appear to secure its investors’ investments and then attach the word mortgage to them for belt and suspenders. These investments were misrepresented to investors, many of which were unsophisticated and who did not receive proper ILA, suitability investigation or other required diligence. The investments themselves were in fact not mortgages but loosely secured equity investments disguised as a mortgage.”

Although, there are numerous variations¹, in a typical syndicated mortgage transaction, a borrower will contact a mortgage broker looking for financing. The mortgage broker will take an application from the borrower and shop the application to different lenders, which are represented by other mortgage brokers.

¹ A mortgage broker might take on a dual role by acting for the both the investor lender and the borrower.

How will Exempt Market Dealers Replace Mortgage Brokers Acting for Investor Lenders?

Mortgage brokers who act for lenders are more than mere salespeople selling a finished mortgage product. The lender's mortgage broker typically will:

- underwrite the mortgage;
- inspect the property, appraisal and other property information;
- issue a commitment letter for the borrower;
- determine conditions for completion;
- ensure that the conditions have been satisfied;
- prepare lender disclosure for the lenders which states mortgage and transaction details; and
- for draw mortgages, ensure that work has been completed before further draws are authorized.

Exempt market dealers are described by the CSA as “sellers” and investor lenders as “purchasers”. However, when it comes to syndicated mortgage lending, mortgage brokers acting for lenders do not sell investments – they arrange, negotiate, structure, confirm and process the mortgage transaction on behalf of the investor lender.

The mortgage broker acting for the borrower engages in a different role from that of the broker assisting the investor lender (unless acting in dual capacity) and will assist the borrower in assessing the transaction, negotiating terms on behalf of the borrower, obtaining the commitment and clearing off commitment conditions.

The CSA proposal appears to assume that a mortgage broker will still be involved in syndicated mortgage transactions, but it is not clear exactly how. Is it contemplated that a mortgage broker representing a borrower looking for syndicated funds contact an exempt market dealer who has investors and who will then provide a mortgage commitment on behalf of the investors?

Here are some questions which the CSA may wish to clarify. If the lenders are no longer assisted by a mortgage broker, but instead by an exempt market dealer, will the exempt market dealer also be:

- underwriting the mortgage;
- drafting the mortgage commitment;
- ensuring that mortgage commitment conditions have been satisfied;
- ensuring that the mortgage is registered appropriately before authorizing the release of lender funds;

- inspecting development sites to determine whether draws are appropriate; and
- educated, trained and tested for competence in all matters relating to mortgage financing, including those matters specified above?

Borrowers are Consumers and Not Issuers

The CSA proposal identifies borrowers in syndicated mortgage transactions as “issuers”² who would need to comply with the requirements of the Securities Act. However, mortgage borrowers are considered under mortgage broker regimes to be consumers deserving of consumer protection measures, and not industry members who must dispense consumer protection to other persons. We are of the view that to catapult the mortgage borrower from consumer to industry service provider under a new syndicated mortgage regime is a serious consumer protection concern which requires further review on an urgent basis.

We are of the further view that it does not make sense for exempt market dealers to turn into syndicated mortgage brokers, when mortgage brokers are already qualified and experienced in this field. The current syndicated mortgage regime in BC with its divided jurisdiction between the Registrar of Mortgage Brokers and the BC Securities Commission and set of exemptions, including the MIE Exemption, works well and should be a model for other jurisdictions to follow. However, if the CSA intends to proceed with its proposal, then we recommend that:

- it develop a broader and more in depth understanding of the mortgage origination process;
- determine how the proposal will impact syndicated mortgage investors and borrowers; and
- explain how gaps in the mortgage origination process will be filled by exempt market dealers.

Thank you for the opportunity to comment on the proposal. Please know that I am available to discuss the CSA proposal further or the comments contained in this letter.

Yours truly,



Samantha Gale, Executive Director, CMBA

² Page 4 of the CSA proposal