FSRA
Financial Services Regulatory Authority of Ontario

Approach

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Supervision Approach for Non-Qualified Syndicated Mortgage Investments with Permitted Clients and Legacy Non-Qualified Syndicated Mortgage Investments

Purpose

This Approach Guidance describes the principles, processes and practices of the Financial Services Regulatory Authority of Ontario ("FSRA") for the supervision of:

- Non-Qualified Syndicated Mortgage Investment ("NQSMI")[1] transactions with investors / lenders that meet the criteria for categorization as "Permitted Clients" effective March 1, 2021;
- NQSMI transactions with Permitted and non-Permitted Clients transacted prior to March 1, 2021 ("Legacy NQSMIs"); and
- Administrators of NQSMIs.

A definition of "Permitted Client" is provided for in section 1 of Ontario Regulation 188/08 – Mortgage Brokerages: Standards of Practice ("O. Reg. 188/08") under the *Mortgage Brokerages, Lenders and Administrators Act, 2006* ("MBLAA"). The definition lists several types of "Permitted

[1] NQSMIs are syndicated mortgages that do not meet the definition of "qualified syndicated mortgage" in accordance with s. 1(2) and 1(3) of O. Reg. 188/08.

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Clients", which are entities and individuals that are presumed to have significant experience and knowledge regarding financial matters, including investments, and robust financial means.[2]

Scope

This Approach Guidance applies to:

1. Mortgage brokerages dealing and trading in NQSMIs with Permitted Clients;
2. Mortgage brokerages, when dealing in NQSMIs, acting on behalf of the borrower in NQSMIs with investors / lenders that are non-Permitted Clients;
3. Mortgage brokerages that dealt and / or traded in Legacy NQSMIs (with Permitted and/or non-Permitted Clients); and
4. Mortgage administrators administering NQSMIs (for Permitted and / or non-Permitted Clients, whether the NQSMIs are Legacy NQSMIs or transacted on or after March 1, 2021).

However, this Approach Guidance does not apply to the supervision of Qualified Syndicated Mortgages[3] (QSMs).

Rationale and Context

NQSMI Regulatory Framework

Effective March 1, 2021, responsibility for regulation of NQSMI transactions is split between the Ontario Securities Commission ("OSC") and FSRA. The division of oversight is based on two elements of NQSMI transactions:

1. Whether the investors / lenders are Permitted or non-Permitted Clients; and
2. The type of activities being conducted with non-Permitted Clients.

[2] This definition of "Permitted Client" reflects the definition used in Canadian Securities Administrators (CSA) National Instrument 31-103.

[3] See footnote 1.

Based on the above, specific oversight activities for NQSMI transactions as of March 1, 2021 will be divided as follows:

A. If the investors / lenders are Permitted Clients, FSRA retains oversight of the dealing and trading in NQSMIs with these investors / lenders as per OSC Rule 45-501.

B. If the investors / lenders are non-Permitted Clients, FSRA retains oversight of the dealing activities with the borrowers, but not of the investors / lenders, as per section 12.1 of Ontario Regulation 407/07. The OSC has oversight of the dealing and trading activities with these investors / lenders in accordance with OSC Rule 45-501.

C. If a NQSMI project involves both Permitted and non-Permitted Clients, the transactions will be overseen jointly by FSRA and the OSC, in accordance with their respective regulatory regimes, as indicated in Table 1 below.

Table 1 – Division of Regulatory Oversight of NQSMIs (as of March 1, 2021)

Investor / Lender Type	Regulatory Oversight	Licence / Registration
Permitted Client	FSRA regulates mortgage dealing and trading in NQSMIs with Permitted Clients. • FSRA oversees dealing and trading activities with both Permitted and non-Permitted Client borrowers and Permitted Client investors / lenders.	FSRA mortgage brokerage licence.
Non-Permitted Client	OSC regulates dealing and trading in NQSMIs with non-Permitted Clients.[4] • OSC has oversight of dealing and trading activities with non-Permitted Client investors / lenders.	Registration with the OSC, or reliance on a dealer[5] registered with the OSC, for trading activities with non-Permitted Client investors / lenders PLUS

[4] OSC also regulates the issuance / issuer of the NQSMI.

[5] E.g., Exempt Market Dealer (EMD), restricted dealer, investment dealer.

	• FSRA has oversight of dealing activities with Permitted and non-Permitted Client borrowers, but not non-Permitted Client investors / lenders. Dealing activities with non-Permitted Client investors / lenders are overseen by the OSC.	FSRA mortgage brokerage licence for dealing activities with Permitted and non-Permitted Client borrowers (soliciting / negotiating / arranging a mortgage).

As described above, MBLAA licensing through FSRA continues to be required for all MBLAA-regulated activities other than dealing and trading in NQSMIs with non-Permitted Client investors / lenders by persons / entities registered with the OSC, or working through a dealer registered with the OSC. These MBLAA-regulated activities include:

- “Dealing” in mortgages, as defined in section 2 of the MBLAA;
- “Trading” in mortgages, as defined in section 3 of the MBLAA;
- “Mortgage lending”, as defined in section 4 of the MBLAA; and
- “Administering mortgages”, as defined in section 5 of the MBLAA.

Depending on the activities being conducted, a person or entity may require a FSRA licence, even though it may also be regulated by the OSC as a dealer.

An OSC registrant selling securities is not exempt from licensing under the MBLAA if engages in any MBLAA-regulated activities such as dealing in mortgages with borrowers or administering mortgages. For example, if an OSC registrant trading in NQSMIs with non-Permitted Clients deals with the borrowers in the same transactions, it must also be licensed with FSRA under MBLAA to work with these borrowers.

Similarly, such an OSC registrant must be a FSRA-licensed mortgage administrator if it wishes to administer a NQSMI or any other type of mortgage.

FSRA Mandate

In supervising and regulating the mortgage brokering sector, FSRA is required to administer and enforce the MBLAA and its regulations in a manner that will achieve FSRA’s statutory objects[6], in particular, to:

- Contribute to public confidence in the mortgage brokering sector;
- Monitor and evaluate developments and trends in the mortgage brokering sector;

[6] See *Financial Services Regulatory Authority of Ontario Act, 2016,* s. 3.

- Cooperate and collaborate with other regulators where appropriate;
- Promote high standards of business conduct;
- Protect the rights and interests of consumers; and,
- Foster a strong, sustainable, competitive and innovative mortgage brokering sector.

Principles

This Approach Guidance describes how FSRA aims to achieve its statutory objects using a data-driven, proactive and targeted, risk-based approach to supervision:

Data-driven judgement – FSRA collects data from mortgage brokerages and administrators to appropriately target supervision of higher-risk brokerages and administrators.

Proactive – FSRA creates forward-looking risk assessments of mortgage brokerages and administrators to implement processes to identify issues early and take actions for timely intervention, as required.

Targeted risk-based approach – FSRA targets its supervision resources based on the risk profile of the mortgage brokerage and administrator and the NQSMIs it transacts and administers, respectively. The risk profiles consider various factors including the following in Table 2:

Table 2 – Risk Profile Factors

Mortgage Brokerages Risks:	• Number of brokers, agents, locations • Compliance history, including complaints received and supervision review outcomes • NQSMI funds raised and number of real estate projects funded
Mortgage Administrators Risks:	• Type of mortgages being administered • Type of investors / lenders in a mortgage • Type of borrower in a mortgage • Non-arm's length relationship with borrower in a mortgage (i.e., related to borrower / not independent of borrower)

NQSMI Risks:	
	• Total mortgage value (amount) • Outstanding balance • Intended use of funds • Project status • Existence of a subordination clause • Type of Permitted Client investors / lenders (e.g., entity versus individual) • Conflicts of interest between parties • High loan-to-value ratios (e.g., 90% of higher) • Location of the subject property

Processes and Practices

Supervision Approach for Mortgage Brokerages Dealing and Trading in NQSMIs with Permitted Clients

The objectives of this supervision approach are to:

- Supervise by monitoring and evaluating developments and trends in NQSMIs with Permitted Clients through regular data collection and adjusting FSRA's supervision approach based on analysis of the data; and
- Ensure mortgage brokerages dealing and trading in NQSMIs with Permitted Clients comply with the MBLAA, its regulations, and applicable FSRA Guidance[7] to ensure adherence with FSRA's statutory objects.

Proactive Review of Quarterly NQSMI Data Report

Subsection 29(2) of the MBLAA gives FSRA broad authority to request information and documents from licensees. Under this authority, FSRA requires mortgage brokerages to provide a quarterly report of the data outlined in Table 3 for each NQSMI with Permitted Clients.

This report must cover the immediate past quarter and must be submitted within ten business days after the end of the quarter.

[7] See Appendix 1 for applicable Guidance.

This quarterly NQSMI data report supplements information collected through the Annual Information Return ("AIR") and replaces the more expanded[8] data submission previously required for FSRA real-time supervision.

While FSRA does not require a similar data report for trades in NQSMIs to non-Permitted Clients, it is made aware of industry conduct issues through various information sharing practices with other regulators. FSRA reviews information from other regulators and takes regulatory action, including enforcement, as may be required.

Examples of compliance or enforcement actions include the imposition of licence conditions, suspension or revocation of licence, and enforcement proceedings seeking administrative monetary penalties.

FSRA also considers this information when determining initial or ongoing suitability for licensing with FSRA and when supervising MBLAA-regulated activities.

Table 3 – NQSMIs with Permitted Clients – Quarterly NQSMI Data Report

Project	Mortgage amount, term, purpose[9], use of funds[10], loan-to-value ratio, ranking, existence of subordination clause
Property	Type of property funded, estimated market value (also referred to as the 'as is' value) of the property, location of the property
Transactions / investments	Investors: Total number of investors, number of Permitted Clients involved, their names, the value of their respective investments, supporting documentation confirming the Permitted Client status and specific category of Permitted Client Borrowers: Borrower class (i.e., level of sophistication)
Mortgage administrator	Name of mortgage administrator

[8] The data that collected via real-time supervision was more restrictive in terms of timing (filing required within five days) and more content-extensive. FSRA is no longer collecting:

- Source of investment funds
- Name of prior mortgagees, if applicable
- Details of appraisals (i.e. name, title and contact information of appraiser etc.)
- Information re: borrowers, developers (if different than borrower) and guarantors' names.

[9] Such as purchase, refinance, construction / development, renewal, renovation.
[10] Such as (raw) land acquisition and/or development, equity take-out, soft and/or hard construction costs, zoning/plans/permits approvals, payout tax liens or mortgage arrears.

Fees	Fees schedule (e.g., for fees received by / owed to the brokerage and related parties)
Related Parties	Actual and / or potential conflicts of interest within a transaction among the mortgage brokerage, the mortgage administrator, the borrower and developer

Targeted Compliance Reviews

Using the quarterly NQSMI data report, AIR, and internal supervisory information, FSRA creates a risk profile for each mortgage brokerage. Mortgage brokerages with a high-risk profile are targeted for increased supervisory oversight such as compliance desk reviews, onsite examinations, or referral to enforcement. Risk profiles are determined according to FSRA's risk framework, in which, individual risk factors are assigned risk values that add up to an overall risk rating.

As part of its compliance reviews, FSRA examines the mortgage brokerage's supervision of its brokers / agents and its policies and procedures, with a focus on the due diligence conducted to ensure investors / lenders for NQSMIs meet the Permitted Client definition.

Mortgage brokerages must take reasonable steps to confirm the Permitted Client status and class of these investors / lenders. These steps must include:

- Documenting the steps taken to confirm investor / lender status; and
- Obtaining signed confirmation of Permitted Client status from the investor / lender.

Review findings could result in follow-up compliance or enforcement actions[11], as appropriate.

Supervision Approach for Mortgage Brokerages that Dealt and/or Traded in Legacy NQSMIs

As noted earlier, Legacy NQSMIs are NQSMIs with Permitted and non-Permitted Clients transacted by mortgage brokerages prior to March 1, 2021. The objectives of this supervision approach are to:

- Supervise by monitoring and evaluating the status and recoverability of Legacy NQSMIs through at least annual data collection;

[11] Examples of compliance or enforcement actions include, without being limited to, the imposition of licence conditions, suspension, revocation of licence, and enforcement proceedings seeking administrative monetary penalties.

- Ensure mortgage brokerages with Legacy NQSMIs complied with the provisions of the MBLAA and its regulations, and applicable FSRA Guidance[12] in place prior to March 1, 2021; and
- Protect the rights and interests of NQSMI investors / lenders and borrowers.

Data-driven, Targeted Compliance Reviews

Through periodic surveys[13], FSRA will collect data, such as that outlined in Table 4, from select mortgage brokerages to monitor and evaluate the residual risk to investors / lenders and borrowers in Legacy NQSMI transactions.

[12] See Appendix 1 for applicable Guidance.
[13] Data collection surveys will be completed on at least an annual basis.

Table 4 – Data Collection for Legacy NQSMIs

Project	Project, status, outstanding loan amount, loan-to-value ratio
Property	Type of property funded (e.g., residential, commercial, mixed-used, industrial), estimated market value (also referred to as the 'as is' value) of the property, location of the property
Transactions / investments	Investors: Total number of investors, investor type (designated or other), their names, the value of their respective investments, supporting documentation confirming the designated investor status and category of designated investor Borrowers: Borrower class (i.e., level of sophistication)
Mortgage	Whether the term was extended past the contractual extension date and how many instances If the mortgage was paid out, if investors / lenders were paid out in full
Mortgage administrator	Name of mortgage administrator
Fees	Fees schedule (e.g., for fees received by / owed to the brokerage and related parties)
Related Parties	Actual and / or potential conflicts of interest within a transaction among the mortgage brokerage, the mortgage administrator, the borrower and developer
Disclosures	What disclosures were made and by which party
Exit strategy	How investors / lenders will be repaid

Using the Legacy NQSMIs data collected, AIR and internal supervisory information, FSRA creates a risk profile for each mortgage brokerage.

For Legacy NQSMIs with greater risk of investor / lender loss, FSRA will conduct further reviews to understand, at a minimum:

- Disclosures provided to investor / lender consumers by the mortgage brokerage; and
- Suitability assessments conducted on investor / lender clients throughout the life of the NQSMI where the funding is completed in various raises / tranches.

This approach reflects FSRA's existing supervision of mortgage brokerages that dealt and traded in NQSMIs prior to March 1, 2021.

Supervision Approach for Mortgage Administrators Administering NQSMIs

The objectives of this supervision approach are to:

- Ensure mortgage administrators administering NQSMIs comply with the MBLAA, its regulations, and applicable FSRA Guidance; and
- Ensure the protection of investor / lender interests, in particular, the interests of non-Permitted Client investors / lenders.

Desk Reviews of Mortgage Administrators Administering NQSMIs

FSRA's supervisory approach for mortgage administrators that administer NQSMIs focuses on the administration of NQSMIs with non-Permitted Clients.

Using AIR and internal supervisory information, FSRA creates a risk profile for each mortgage administrator. Mortgage administrators with a high-risk profile will be targeted for increased supervisory oversight such as compliance desk reviews, onsite examinations, and referral to enforcement where applicable. Risk profiles are determined according to FSRA's risk framework, individual risk factors are assigned risk values that add up to an overall risk rating.

As part of its compliance reviews, FSRA will examine the mortgage administrator's:

- Steps taken to ensure it is aware of subsequent encumbrances and significant changes in circumstances affecting the mortgage (see Guidance No. MB0039INT);[14]
- Notifications provided to investors / lenders;[15]
- Disclosures, and timing of disclosures, made to each investor / lender, in particular:
  - Disclosure of the mortgage administrator's relationships with each borrower, as per section 19 of Ontario Regulation 189/08 – Mortgage Administrators: Standards of Practice (O. Reg. 189/08).
  - Disclosure of any conflicts of interest that the mortgage administrator or an employee administering the mortgage may have in connection with the mortgage as per section 20 of O. Reg. 189/08.
- Processes and controls for the exercise of discretion;[16] and

[14] See FSRA's Mortgage Administrators – Responses to Market Disruption Interpretation Guidance No. MB0039INT (Guidance No. MB0039INT).
[15] See footnote 14.
[16] See footnote 14.

- Processes and controls to ensure concurrent businesses (if any) do not jeopardize its integrity, independence or competence when carrying on the business of administering mortgages as per section 40 of O. Reg. 189/08.

Review findings could result in follow-on compliance or enforcement actions,[17] as appropriate. Maladministration of NQSMIs, or improper behaviour towards a borrower in a NQSMI, could result in FSRA bringing sanctions under the MBLAA.

Effective Date and Future Review

This Approach Guidance is effective March 1, 2021 and will be reviewed no later than March 1, 2024.

About this Guidance

This document is consistent with FSRA's Guidance Framework. As Approach Guidance, it describes FSRA's internal principles, processes and practices for supervisory action and application of Chief Executive Officer discretion. Approach Guidance may refer to compliance obligations, but does not in and of itself create a compliance obligation.

[17] Examples of compliance or enforcement actions include, without being limited to, the imposition of licence conditions, suspension, revocation of licence, and enforcement proceedings seeking administrative monetary penalties.

Appendix

This Appendix outlines the applicability of FSRA Guidance to NQSMI transactions.

Applicability of FSRA Guidance and Forms			
Issue Date	**Guidance**	**For NQSMI transactions on or after March 1, 2021 Applies to:**	**For NQSMI transactions before March 1, 2021 Applied to:**
May 12, 2020	Mortgage Brokerage Disclosure and Suitability Assessments for Non-Qualified Syndicated Mortgage Investments (SMIs) – Responses to Market MB0040INT	NQSMIs with Permitted Clients[18]	Legacy NQSMIs
May 12, 2020	Mortgage Administrators – Responses to Market Disruptions MB0039INT	All Mortgage Administrators	All Mortgage Administrators
December 5, 2019	Amended disclosure forms 3.0, 3.1 and 3.2 for non-qualified syndicated mortgages MB0038INT	Not applicable	Legacy NQSMIs
December 5, 2019	FAQs about Forms 3.0, 3.1 and 3.2 Amended Disclosure Forms for Non-Qualified Syndicated Mortgages MB0025ORG	Not applicable	Legacy NQSMIs

[18] On or after March 1, 2021, all Permitted Clients can waive the suitability assessment; non-Individual Permitted Clients are exempt from the following disclosures:

- Role of brokerage (s.18 of O. Reg. 188/08);
- Brokerage's relationship with lenders (s. 19 of O Reg. 188/08);
- Disclosure of brokerage's relationships (s. 26 of O. Reg. 188/08); and
- Disclosure of conflicts of interest or potential conflicts of interest (s. 27 of O. Reg. 188/08).

November 12, 2019	Supervision approach for high-risk syndicated mortgage investments MB0037APP	Not applicable	High-Risk Legacy NQSMIs
October 26, 2018	Policies and Procedures - Non-qualified Syndicated Mortgages MB0009ORG	Not applicable	Legacy NQSMIs
Effective July 1, 2018	Checklists for Non-Qualified Syndicated Mortgage Forms effective July 1, 2018 MB0024ORG	Not applicable	Legacy NQSMIs
June 28, 2018	Changes to syndicated mortgage rules: New FSCO forms available MB0008ORG	Not applicable	Legacy NQSMIs
June 30, 2015	Requirements for Promoting Syndicated Mortgage Investments MB0006ORG	NQSMIs with Permitted Clients	Legacy NQSMIs
January 21, 2015	MFDA and FSCO issue joint communication concerning the selling of syndicated mortgage investments MB0017ORG	NQSMIs with Permitted Clients	Legacy NQSMIs