Vector Financial
SERVICES LIMITED
Brokerage Licence #10160, Administrator Licence #11205

Vector Financial Services Limited (*Vector Financial*) Response to call for Comments August 6, 2020
Amendments to National Instrument 45-106 *Prospectus Exemptions* and National Instrument 31-103
Registration Requirements, Exemptions and Ongoing Registration Obligations

AND

Changes to Companion Policy 45-106CP *Prospectus Exemptions* and Companion Policy 31-103CP
Registration Requirements, Exemptions and Ongoing Registration Obligations

September 21, 2020

To: **Ontario Securities Commission**
20 Queen Street West
Toronto, Ontario M5H 3S8
Attention: The Secretary
comments@osc.gov.on.ca

Financial Services Regulatory Authority of Ontario
5160 Yonge Street, 16th Floor
Toronto, Ontario M2N 6L9
Attention: Huston Loke, Executive Vice President, Market Conduct
Huston.Loke@fsrao.ca

Ministry of Finance
Financial Services Policy Division
Attention: Gina Stephens, Senior Policy Advisor
Gina.Stephens@ontario.ca

Dear Sirs and Madam,

Thank you for including **Vector Financial** in the group of companies that will be making comments to these proposed amendments and for organizing the teleconference on September 15 in which we were allowed to present some comments on the regulatory direction regarding Non-Qualified Syndicated Mortgage Investments (NQSMI). These matters are extremely relevant and important to us as over 95% of our revenues are derived from the brokering, lending, and administration of NQSMI's. Our firm dates back to 1970 and we currently serve over 400 investors and administer a book of loans of approximately $275 million and complete 20-24 loans per year. We employ twelve individuals to carry out our mandate.

We recognize that not all market participants engaged in NQSMI's have acted in the best interest of their investors or the public, and it is not surprising that some revisions are being made to the governance of NQSMI's to incentivize market participants to raise their standards of behaviour. In fact, we welcome this, as we are proud of how we govern ourselves and want to ensure other participants do not give our sector a bad name. Having said that, we have reviewed the proposed comments, and while we are in agreement with most of the initiative, we have the following comments we hope you will consider favourably.

Carve Out of "Permitted Clients" under FSRA

While we understand the impetus behind this proposal, this particular item causes the most issues for us, as it requires us to report in two jurisdictions; the OSC and FSRA. Both Permitted Clients and Accredited Investors fund the majority of our loans and to follow the rules as written would require us to send different documentation to different lenders in the same loan and to keep track of who gets what. In our opinion, all individual investors as well as entities controlled by them should be under one regime.To simplify this we suggest a couple of alternatives.

- Broaden the Carve Out to include both Permitted Clients and Accredited Investors. In our case this describes over 95% of our investors and we would consider ways to accommodate the other 5% or part ways with them; or

- **Allow firms to choose if they want their Permitted Clients regulated by the OSC or by FSRA and subject them to disclosure standards of that regime.** It is not clear if this is permitted in the current proposed language. By allowing this to occur, a firm such as **Vector Financial** can transfer their entire investor regulatory burden to the OSC (if they choose to), which reduces duplicate record keeping. We are not suggesting avoiding regulatory oversight; just to simplify it.

There are clear benefits to this:

- Firm's investor disclosures and KYCs are governed by one regulator and not two in keeping with the Ontario government's mandates of reduced paperwork burden for market participants
- Eliminates the need for our sales people to be dual licensed as mortgage agents (FSRA) and dealing representatives (OSC) to deal with clients on the same loan
- Avoids potential errors in reporting investor information to the wrong regulator.
- Ensures better investor privacy as confidential information is only shared once
- Avoids the duplication of E & O insurance premiums – a costly part of our business with premiums current over $25,000 for FSRA alone.

Filing of Report Exempt Distribution (Report)

Under current FSRA regulations, we are required to file our investment summary (our version of an OM) and remit a $200 fee within 5 days of the distribution of this document to the first investor. As we process 20 to 24 loans per year, this equates to between $4,000 to $4,800 per year and this is a reasonably new cost to our business that was introduced in the past 12-18 months. Under the current proposal, in addition to the above, we will now have to file Form 45-106F1 within 10 days of a distribution and pay $500 each time; this would add a further new cost of $10,000 to $12,000 to our business per year. To avoid this we make the following suggestions:

- The OSC reduces the fee to $200 per occurrence and if filed with the OSC relieves the participant of also filing with FSRA; or

- Allow us to file monthly/quarterly reports and include whatever trades were distributed in that period and pay the fee only one time. We understand the investment managers running hedge funds are required to only remit their trades on an annual basis so there is precedent for this.

Administrator Oversight:

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.

Disclosure made as part of the original OM or other provision under OSC should be considered sufficient for FSRA's oversight.

Specific Comments to Annex "A" Summary of Comments and Responses

Transition Period: Comment 8

Consider eliminating (or grandfathering) alternative prospectus exemptions for retail investors on loans that originated prior to March 1, 2021 but which have future advances after that date. Otherwise, one loan is in two regimes and this does not appear necessary or efficient. The reality is there will not be too many of these.

Reports of Exempt Distribution: Comment 25

Consider eliminating the requirement for filing multiple reports of exempt distribution on loans with multiple advances over the course of the loan (i.e. construction). <u>In most cases, the fundamental disclosure to investors has been made at the front end</u>. The timing of advances is for the benefit of the borrower and reduces interest costs during the construction term. These future advances are not new reasons to raise capital such as secondary or follow on offerings, which occur in the public markets.

Identifying the Issuer of a Syndicated Mortgage: Comment 27

It is still unclear who the issuer of an NQSMI is under the current regulation. It seems to be circumstances dependent. We believe that in almost 100% of the cases a firm like ours would be considered the issuer and we would be governing ourselves accordingly and accepting the regulatory risk. We want to avoid situations where the regulator takes a different position and imposes burdens on our borrowers that were unexpected, difficult to manage and costly.

Appraisals: Comment 30

In addressing comments that were raised during the September 15 zoom tele-conference, we strongly suggest that the requirement for a 6-month appraisal be reconsidered and that the regulator leave the 12-month dating in place. As mentioned on the call, many construction projects take more than 12 months to complete and if the 6-month appraisal time period is in place this may require 2 or 3 appraisals to be done during one construction project. The more relevant document during the construction phase are the quantity surveyor reports that precede each construction advance and give information to the lender about any risks arising during construction. In addition, it is unclear who will pay this added cost, as well as the difficulty for an appraiser actually determining the "as is" value at a specific point in time during construction, the alluded protection to investors and the public is questionable. Without prior training in property valuation, an ordinary member of the public cannot make use of the information in the appraisal so it is unclear how they are truly protected.

Audited Financial Statements: Comment 39

We have consistently brought up the point that we find this requirement a real burden on our borrowers and of no actual benefit to investors. To re-iterate, most of the borrowers are single purpose, non-operating entities whose essential asset is land and the ongoing costs (which are then capitalized) associated thereon. In many cases, the borrowing entity is only established within the preceding 90-180 days of the initial transaction and has no previous operating history.

Recommendation: remove this requirement for audited statements, revert to Notice to Reader statements and leave the disclosure of the financial condition of the borrower to investors to be the responsibility of the broker/administrator in whatever form they consider under the specific circumstances of a loan. This can also be replaced by the credit report of the guarantor if necessary.

I hope you will consider these comments in a favourable light. I am available to further discuss the above matters if requested at any time.

Respectfully submitted.

Vector Financial Services Limited

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Mitchell Oelbaum, Chief Operating Officer
FSRA Mortgage Agent M13001562