CFA Societies Canada

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September 21, 2020

VIA EMAIL

Corporate Secretary
Financial and Consumer Services Commission
85 Charlotte Street, Suite 300
Saint John, N.B.
E2L 2J2
E-Mail: info@fcnb.ca

Dear Sirs/Mesdames:

Re: Proposed Local New Brunswick Amendments to Commission Rule 45-501 *Prospectus and Registration Exemptions* relating to Syndicated Mortgages (the "Proposed Amendments")

The Canadian Advocacy Council of CFA Societies Canada[1] (the "CAC") appreciates the opportunity to provide the following comments on the Proposed Amendments.

As noted in our prior comment letters to the CSA with respect to the amendments to National Instrument 45-106 *Prospectus Exemptions* and National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103"), we generally support the broader changes being made to the prospectus and registration exemptions for syndicated mortgages as a result of the inherent risks associated with distributing such products to retail investors.

We were also supportive of the harmonization that the removal of the exemptions would achieve, being cognizant of the fact that mortgage brokerage legislation is not uniform in every jurisdiction. While we would generally prefer that the exemptions were the same in each province and territory, we do not object to the expansion of those exemptions in New Brunswick.

We understand that the Proposed Amendments are intended to clarify the definition of a "qualified syndicated mortgage", as well as provide additional registration and prospectus exemptions related to the distribution of certain mortgages. Subsequent

[1] The CAC is an advocacy council for CFA Societies Canada, representing the 12 CFA Institute Member Societies across Canada and over 18,000 Canadian CFA charterholders. The council includes investment professionals across Canada who review regulatory, legislative, and standard setting developments affecting investors, investment professionals, and the capital markets in Canada. Visit www.cfacanada.org to access the advocacy work of the CAC.
CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Our aim is to create an environment where investors' interests come first, markets function at their best, and economies grow. There are more than 177,600 CFA charterholders worldwide in 165 markets. CFA Institute has nine offices worldwide and there are 160 local member societies. For more information, visit www.cfainstitute.org.

to all the amendments, qualified syndicated mortgages will continue to be regulated under the *Mortgage Brokers Act* (New Brunswick), and thus the definition of a "qualified syndicated mortgage" is key, as it is intended to be limited to lower-risk mortgages primarily on residential properties.

We agree that the scope of the definition should be limited. We also support the proposed new exemption for syndicated mortgages sold to permitted clients, as well as the proposal to use the definition for "permitted client" currently found in NI 31-103 so that the waiver of suitability requirements applying to distributions of other securities could also apply to distributions of syndicated mortgages.

We believe the definition of a "qualified syndicated mortgage" should be the same throughout the CSA rules as well as in the rules relating to mortgage brokers in New Brunswick, and in other provinces and territories respecting their mortgage brokerage regulation. Currently, it is proposed that the definition in the province will exclude mortgages with a loan-to-value ratio of greater than 80%, subject to certain calculation provisions. We believe that threshold is set too high.

The fair market value of a property can be volatile and depends on a variety of factors, including interest rates, the unemployment rate, and debt-to-income ratios. When a default occurs on a mortgage loan, the net proceeds from the sale of a mortgaged property will be reduced by a number of items, including unpaid realty taxes and the accrual of interest from the time of default to completion of property sale, as well as real estate broker sales commissions (plus taxes). The value may also be negatively impacted by deferred maintenance and by the loss in value resulting from the property being owned by a defaulting borrower (i.e. reputational stigma). The total loss in the value of the property as a result of these items can amount to greater than a 20% loss, which could lead to a loss of principal for the lender, compounded further if the lender is subordinated to others.

Based on data available from the Teranet-National Bank National Composite House Price Index™ , there was a decline of more than 5% in housing prices between 2009 and 2010 in a recessionary period[2].

In the current pandemic environment, setting the LTV threshold at 90% for syndicated mortgages is particularly risky, as prices could fall quickly leading to a loss of principal (and interest) on a mortgage loan with a 90% LTV ratio.

To provide an illustrative example:

Value of property before price decline:	$100
Mortgage loan	: $ 90
LTV (%)	: 90%
Value of property (after 5% decline)	: $ 95

[2] *House Price Index, Selected Composite 11,* online: House Price Index, Teranet and National Bank of Canada < https://housepriceindex.ca >

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Unpaid realty taxes, realty broker commission and other costs (e.g. capex)	:($ 10)
Net sale proceeds:	: $ 85
Amortized balance of mortgage loan (if amortization)	: $ 88
Net loss to mortgagee	: $ 3

It would therefore be more prudent to lower the LTV threshold in the definition of a "qualified syndicated mortgage" to 75%, which is typically the maximum level used by conventional (uninsured) mortgage lenders.

With respect to the reports of exempt distribution, we do not believe an exemption should be available under securities regulation for distributions of qualified syndicated mortgages or syndicated mortgages sold to permitted clients unless equivalent reports of such trades are in fact requirements under the *Mortgage Brokers* Act (New Brunswick) and collected by regulators. It is important that a regulatory body collects this data for oversight purposes and use these private placement (or similar) reports to track marketplace activity, and there does not appear to be any rationale to treat these distributions differently than those of any other securities.

We understand that the different prospectus exemptions that will be available across the country are in part as a result of the differences in provincial securities and mortgage regulation. We support and commend ongoing efforts to collaborate with other provincial regulators. We continue to encourage the CSA and its various member jurisdictions' other regulators to seek harmonization of prospectus and registration exemptions whenever possible, and reduce duplicative regulation to help ease the compliance burden on issuers and registrants and improve understanding of the syndicated mortgage market amongst investors and other market participants.

Concluding Remarks

We thank you for the opportunity to provide these comments. We would be happy to address any questions you may have and appreciate the time you are taking to consider our points of view. Please feel free to contact us at cac@cfacanada.org on this or any other issue in future.

(Signed) *The Canadian Advocacy Council of*
CFA Societies Canada

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