

August 21, 2014

Introduction

ASC staff advise that they intend to ask the Commission to issue a designation order under section 10(1)(e) of the *Securities Act* (Alberta) (the Act) on or about September 22, 2014 to clarify how various rules applicable to investment funds apply to certain mortgage investment entities that are investment funds as defined under the Act.

Background

The term mortgage investment entity or MIE is generally used to refer to an issuer whose primary business is to directly or indirectly invest all or substantially all of its assets in debts owing to it that are secured by a hypothec or other security interest on real property (Mortgages) and directly or indirectly, involves originating or acquiring and then administering the Mortgages with the intent of holding the Mortgages for their term and using the revenues generated from them to provide a return to investors.

In CSA Staff Notice 31-323 *Guidance Relating to the Registration Obligations of Mortgage Investment Entities*, ASC staff indicated that they consider certain mortgage investment entities or MIEs to be ‘non-redeemable investment funds’, and therefore ‘investment funds’ as defined under the Act.

Disclosure requirements

Although an MIE may meet the definition of a non-redeemable investment fund under the Act, given the nature and structure of the business carried out by certain MIEs, i.e., “Operational MIEs”, as defined in the Annex to this notice, ASC staff have generally considered the provisions of Alberta securities laws, other than those relating to the registration requirement, to be more appropriate for Operational MIEs.

Operational MIEs are those MIEs whose primary business activity is mortgage lending, that is, operating a business that creates and manages mortgages. Factors that we have considered relevant to determining whether or not an MIE is an Operational MIE include the following:

- whether the MIE originates Mortgages in its own name, directly, through an agent acting on behalf of the MIE, or through a third party that originates a material portion of the mortgages financed by the MIE;
- whether the MIE directly or indirectly funds the Mortgages in its portfolio; and

- whether the MIE administers the mortgages, either directly or through an agent acting on its behalf.

ASC staff have generally expected Operational MIEs to file a prospectus in the form applicable to a non-investment fund and to thereafter provide the continuous disclosure, including that prescribed by National Instrument 51-102 *Continuous Disclosure Obligations* applicable to non-investment funds. Similarly, we would not generally think it appropriate that National Instrument 81-102 *Investment Funds* or the requirements under National Instrument 45-106 *Prospectus and Registration Exemptions* directed at investment funds apply to Operational MIEs.

Summary of Designation Order

Because an Operational MIE may be an investment fund under the Act but in circumstances, other than relating to the registration requirement, it is considered more appropriate that such MIEs be subject to the rules applicable to non-investment funds, ASC staff intend to request that the Commission issue a designation order designating Operational MIEs to not be non-redeemable investment funds.

The designation order is expected to provide that, except for the registration requirement, Operational MIEs are designated not to be a non-redeemable investment fund.

Purpose of Designation Order

Designating Operational MIEs to not be non-redeemable investment funds is intended to:

- address issues arising from proposed amendments to National Instrument 81-102 *Investment Funds* (NI 81-102) which are to come into force on September 22, 2014, including
 - avoiding the application of investment restrictions in NI 81-102 to Operational MIEs,
 - clarifying the continuous disclosure requirements applicable to Operational MIEs; and
- clarify the treatment of Operational MIEs under Alberta securities laws, including
 - the prospectus form applicable to an Operational MIE,
 - the prospectus exemptions available to an Operational MIE,
 - the filing deadline for reports of exempt distribution filed by an Operational MIE and

- in the event proposed amendments relating to the required form of reports of exempt distribution become effective, the form of report of exempt distribution to be used by an Operational MIE.

Transition

ASC staff recognize there may be Operational MIEs currently complying with the requirements under Alberta securities laws applicable to investment funds. Staff are prepared to consider recommending on a case-by-case basis, applications for temporary exemptions e.g., to allow an Operational MIE to transition from National Instrument 81-106 *Investment Fund Continuous Disclosure* to National Instrument 51-102 *Continuous Disclosure Obligation*.

Comments

If you have comments on the proposal to designate Operational MIEs not to be non-redeemable investment funds, other than comments in respect of the application of the registration requirement to MIEs, please send them to the following:

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Written comments may be posted on our website. Accordingly, you should not include any personal information in them.

Annex

- (a) “MIE” means an issuer to which each of the following apply:
 - i. it invests substantially all of its assets in Mortgages relating to debts owing to it or to an affiliate of it; and
 - ii. its primary purpose or business activity involves directly or indirectly, originating or acquiring and then administering Mortgages with the intent of holding them for their term and using the revenues generated from them to provide a return to its investors;
- (b) “Mortgage” includes a debt secured by a hypothec or other security interest on real property;
- (c) “Operational MIE” means an MIE, other than an MIE whose primary activity is managing an investment portfolio that includes mortgages, whose business activity is the operation of a business that directly, or through an agent, affiliate, or Principal Originator involves all of the following:
 - i. taking an active role in originating Mortgages;
 - ii. acting as a mortgagee or otherwise providing the funds for Mortgages;
 - iii. administering Mortgages;
- (d) “Principal Originator” means a person or company that originates a material portion of the Mortgages held by an MIE.