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LEADING MAGAZINE FOR ALTERNATIVE LENDING & INVESTING INFORMATION

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RAISE AND MANAGE MIC INVESTMENTS

WHILE MEETING CANADIAN COMPLIANCE REGULATIONS

Mortgage Investment Corporations (MICs) are equity vehicles that finance private mortgages as an alternative mortgage financing from traditional banks. In order to be a successful, MIC Managers will underwrite and manage good mortgages. However, another important requirement for creating and managing a MIC is the ability to raise and manage investments while continuing to meet Canadian compliance regulations.

MIC Managers must maintain compliance for investments according to each provincial security regulators, be able to report to your investors, maintain real time accounting, maintain ongoing transactions such as dividends or interest payments and correctly report to regulatory bodies including issuing T5s for the CRA.

MIC Managers should have a team in place that is versed in Investor regulations such as a Compliance Officer, corporate lawyer, accountant and ideally a software administration system robust and versed it the regulations of MIC investors to ensure growth but most importantly to maintain corporate compliance.

PROVINCIAL SECURITY REGULATIONS, EXEMPTIONS & NATIONAL INSTRUMENT 45-106

When raising capital, MICs fall under each provincial security regulator as well as under an exception under securities law. Reliance on an exemption to raise monies (in most cases) requires a report to the provincial commission depending on where the investor is located and the same report in the province the MIC is located.

MIC Managers can raise money under an Exemption defined under the provincial securities act, regulations and national instruments. For example, National Instrument 45-106 provides for the details in which a company can raise money under an exemption from prospectus and dealer registration.

MICs fall under the Common Prospectus Exemptions which Include:

- Accredited Investor: Those investors who are sophisticated or deemed to be, such as institutions, governments, persons or companies who meet an income and asset test. Please refer to KYC or Know Your Client regulations.
- “Private Issuer” or Closely-held Issuer Exemption: The shares are all subject to restrictions on transfer found in the Articles of Incorporation, and all the shares cannot be owned by more than 50 persons, not including employees, former employees, or corporate affiliates. The purchasers must be a director/officer/employee of the MIC or Affiliate of the MIC, or close family, friends and business associates of those individuals, or an accredited investor. Except when selling to an accredited investor, no commissions or finder’s fees can be paid to the director/officer/employee of the MIC.
- Family, Friends and business associates: Except in Ontario and modified in Saskatchewan, the definition is pretty broad and are limited to 50 shareholders in total.
- Founder, control person and family: Applies only in Ontario and much narrower definition of the Family, Friends and Business associates.
- Offering memorandum.
- Minimum amount investment: The purchase price for the shares is at least $150,000 in total paid in full at the time of distribution.

EMD AND KYC AND FORM 45-106

According to the Ontario Securities Commission, “if a MIC is found to be actively in the business of raising monies as a private non-public (not listed on an exchange) corporation continually relying on an exemption, the MIC may also be required to register as an exempt market dealer (“EMD”) or only raise funds through the use of an EMD. Registering as an EMD will also mean strict governance and substantial errors and omissions insurance among other compliance requirements regulated by the applicable provincial commission such as the Ontario Securities Commission (OSC).”

KYC or Know your Clients is a vetting process by MIC Managers to ensure that their investor is risk tolerant to MIC investment. Most MIC Managers will create and maintain their unique process and will generally involve a workflow of qualification (income verification for instance).

OSC states that "companies and underwriters must report certain exempt distributions to the OSC by completing and filing Form 45-106F1 Report of Exempt Distribution (Form 45-106F1) through the OSC's Electronic Filing Portal Portal and pay the applicable filing fee. Form 45-106F1 must be filed no later than 10 days after the distribution. Investment funds relying on certain prospectus exemptions have the option of filing Form 45-106F1 on an annual basis, within 30 days of the end of the calendar year."

Form 45-106F1 must be filed electronically for distributions under:

- section 73.3(2) of the Securities Act (Ontario) [Accredited investor]
- section 73.5(2) of the Securities Act (Ontario) [Government incentive security]
- certain prospectus exemptions in National Instrument 45-106 Prospectus Exemptions
- Multilateral Instrument 45-108 Crowdfunding

A new Form 45-106F1 Report of Exempt Distribution came into force on June 30, 2016 and MIC Managers should ideally have an electronic system in place to produce the supporting documents including the detailed excel report required attachment.

REPORTING REQUIREMENTS

MICs under the The Client Relationship Model - Phase 2 (CRM2) amendments to NI 31-103 that came into effect on July 15, 2013 define new requirements for reporting to clients about the costs and performance of their investments, and the content of their accounts.

According to OSC, "an account statement has two principal elements: transactional information and account position information. Transactional information is specific to the securities involved and is required in almost all circumstances where there has been a transaction. Account position information is a snap-shot of the whole account and is required only where the firm holds client assets." MIC Managers should have a robust system in place to maintain records on both the original investment with a certificate as well as the related transactions such as deposits, dividends, transfers and redemptions. A system should integrate all the MIC certificate investments to the investor account rather than having separate accounts for each investment. Reports include cost disclosure, performance reporting and client statements such as Quarterly Statements and Statement of Holdings.

TYPES OF INVESTMENTS

MIC Managers can raise private equity though investors both from individuals, trusts, joint accounts, registered accounts, non-registered, agents and corporate investments.

Types of Investment can be in Cash (individual, joint, trustee or corporate) as well as registered capital with a Trustee. MIC capital can also be raised through third party including EMD (exempt market dealers) and financial advisors. Some MICs also raise capital from Investors residing outside of Canada (non-resident) but will must comply with non-resident compliance, taxes and reporting.

REGISTERED ACCOUNTS

An excellent source of capital for MICs is registered funds held at a Trustee. With the Trustees approval for holding the investments of a MIC, MICs now have an excellent source of investors capital while investors can receive a more substantial return than conservative

investments held within a registered account. For new MICs it is recommended to contact Olympia Trust, Canadian Western Trust and Community Trust for more detail.

In order for a MIC to have registered accounts they must comply to the rules set by the Trustee after they have been approved by the Trustee. Once approved, MICs will generally be able to accept all registered accounts including RRSP, RRIF, LIRA and TFSA.

MIC Managers will be required to report to Trustees in the method determined by the Trustee. For example, Olympia Trust recently changed their policy for MICs to submit a global certificate as opposed to the 100s of individual certificates. Similarly, Trustees will require the correct reports for cash distributions for dividends and any changes in the registered account.

THIRD PARTY

Some MICs are using third party sources to raise capital such as financial agents and through 3rd party firms such as Fundserve. Although agencies such as Fundserve will provide exposure to different potential investor segments, these options are costly on a monthly basis and could be prohibitive for growing and smaller MICs.
MICs with over 50 investors can also advertise in publication and trade show to publicly promote investor opportunities. Internet based investor raising (crowd funding) can be of value and MIC Managers can always contact technology and software suppliers for more detail.

MANAGING INVESTORS

Once a MIC raises the capital, they will need to manage their investors transactions. The primary transactions for MIC investors are redemptions, transfers and most importantly dividend calculations and distributions. Having a system in place for dividend calculations and distributions will save days of administration time and significantly reduce errors. Similarly, a system for distributions will allow MIC Manager to send EFT payments directly to investors, calculate and manage Trustee distributions, maintain compliance and create and send investor reports by mail, email and for online statements.

T5S

MIC Managers will need to issue T5s to the investors. Many MICs will not issue T5s to registered accounts as the Trustees manage registered investors directly. For a MIC with over 50 investors, MIC Managers must submit T5s electronically direct to CRA and thus need to ensure the information is accurate and complete.

GENERAL MIC COMPLIANCE

1. A financial audit (completed by a qualified firm CA or CPA firm, does not need to be IFRS, as MICs are not automatically considered reporting issuers even though they are deemed "public companies" under the Canadian Income Tax Act);
2. Annual resolutions to approve the financial statements;
3. Annual resolutions to declare dividends, and possibly to catch up for dividends declared throughout the year on a monthly or quarterly basis;
4. Annual resolutions to declare any bonuses to the officers and managers;
5. Resolutions to effect any issuance of shares to new investors, and possibly to catch up for shares issued throughout the year to investors;
6. Reporting Requirement for Exempt Distributions (i.e. for issuing shares to investors under an exemption such as the "Accredited Investor"), in the jurisdiction where the distribution/issuance takes place (e.g. Ontario) a form 45-106F1 for Investment Funds (e.g. a MIC can be considered an Investment Fund if it does not exhibit any control over the private companies it invests in that are in addition to the mortgages invested in or directly funded), is required to be filed with the provincial securities commission within 30 days after the MIC's financial year-end if the exemption used was either an Accredited Investor, Minimum Amount or Additional Investment in Investment Funds, otherwise (i.e. not considered an investment fund and has not distributed/issued shares to investors under the previously mentioned exemptions) it needs to be filed within 10 days after the distribution/issuance.
7. MIC Managers will need to file the Form 45-106 based on managed certificates within 10 days of share purchases

Raising Capital for MICs is essential for maintaining a MIC. When creating a MIC, having the correct contracts such as a subscription agreement are the first step. Recognizing various different sources of capital such as registered funds will also provide growth. Most importantly, having a system to comply to regulations and each provincial security regulation is vital as any errors are extremely costly and can cost the MIC their business. MIC Management on the Investor component is just as important as ensuring the MIC is underwriting the best loans.

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Shannon Dolphin is CEO of Dolphin Enterprises Ltd. and has been working with MICs for over 14 years. Dolphin and its new Underwriting and MIC Manager software solution is the only software to provide administration for MICs from the application of the loan to the back-end transaction based Chart of Accounts/Accounting system. For more information contact info@dolphinent.com or call 604-685-6721 or visit www.dolphinent.com