INVESTIGATION

Inside the fall of Fortress

Fortress Real Developments raised $920-million from 14,000 Canadians who thought they were getting low-risk, steady income. Now, as the company comes under the pressure of an RCMP investigation and faltering projects, some face the prospect of devastating losses

JANET MCFARLAND REAL ESTATE REPORTER
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Mario Narciso and Fernanda Cortes at their home in Vaughan, Ont., on Nov. 16, 2018.

CHRISTOPHER KATSAROV/GLOBE AND MAIL

By the time the RCMP raided the offices of Fortress Real Developments Inc. on April 13, Mario Narciso and his wife, Fernanda Cortes, had already started to worry they'd made a bad investment.

Four years ago, Mr. Narciso was framing a roof in Toronto when he fell several metres, breaking his spine and leaving him partially paralyzed. Confined to a wheelchair and unable to work, the now 58-year-old received a $500,000 insurance settlement to help support himself, Ms. Cortes and their daughter, now five years old.

The couple wanted to put the money into a safe, income-generating investment but had little experience with investing. An acquaintance introduced them to an adviser well-known in Toronto's Portuguese community, who suggested one of their best options was to invest in a so-called syndicated mortgage, a pool of funds that would help finance early-stage real estate projects.

The adviser, whom the couple did not want identified, recommended a condominium and retail development in Barrie, Ont., known as Collier Centre. Investors in the Fortress-led project could earn 8-per-cent annual interest and would receive their principal back within a maximum of two years, making it a safe investment with a fixed return, the adviser told them. Plus, their loan would be secured by a mortgage against the property, so they would have a registered claim on the land. That was the pitch, anyway.

"He said that the only way it could go wrong was if the real estate market collapsed, which was extremely unlikely at that point," recalls Ms. Cortes, 35.

In 2015, the couple agreed to hand over their whole $500,000 settlement, joining 600 other investors who would collectively pool $36-million for the Collier Centre project.

What Mr. Narciso and Ms. Cortes didn't know was that Collier Centre was just emerging from bankruptcy protection and that a group of earlier syndicated mortgage investors still had not been repaid the $16.9-million they'd put up back in 2012.

"If we had any warning of risk anywhere, we wouldn't have put all our money into this," says Ms. Cortes, who is expecting a new baby in the spring.

They are far from alone. Between 2008 and 2017, Fortress – based in Richmond Hill, Ont., just north of Toronto – raised a staggering $920-million from 14,000 retail investors to fund mortgages for an array of developments, including a dozen condo projects by well-known developer Brad Lamb and Winnipeg's SkyCity, initially billed as the tallest building between Calgary and Toronto.

At its peak, Fortress was Canada's largest syndicated mortgage company. It also led the transformation of what had once been a high-risk investment vehicle for wealthy investors into a mainstream one sold to ordinary Canadians. And as more people handed over their life savings to Fortress and other syndicated mortgage firms – many of which adopted Fortress's retail-investor focus – the provincial mortgage regulator, the Financial Services Commission of Ontario (FSCO), did little to protect them.

Now, Fortress is crumbling. Many of its biggest projects have faltered, and senior lenders are moving to put some of them into receivership. In April, the RCMP searched the company's offices, prompted by complaints from investors about heavy losses on Fortress investments and the fact that they had not been given accurate information on the risky deals.

For its part, Fortress says it has broken no laws, and investors have always been fully informed about all the terms of the investments and their risks. Neither of the company's founders agreed to be interviewed for this story, but in an e-mailed statement, Fortress's lawyer Scott Fenton said: "Fortress is a substantive business with a track record of considerable success led by respected leaders who are committed to bringing maximum value to all investors."

Nonetheless, it looks increasingly likely that Fortress could become Canada's largest syndicated mortgage failure – leaving thousands of investors like Mr. Narciso and Ms. Cortes wondering whether they'll ever see their money again.

Fortress founder and CEO Jawad Rathore is seen leaving the company's office in Richmond Hill, Ont., on Dec. 11, 2018.

FRED LUM/GLOBE AND MAIL

Jawad Rathore is, by all accounts, hard to forget. Tall and bearded, with a shaved head, Fortress's 42-year-old founder, Chief Executive Officer and majority owner likes to spend his money on flashy luxuries. He favours tailored three-piece suits and expensive cars; among his collection are a Ferrari California, a Porsche 911, a Rolls-Royce Ghost Series II and a Range Rover, according to a lien search.

The father of six is also immensely charming, a natural salesman who is most comfortable in front of an audience. At a Fortress professional development event at Toronto's Winter Garden Theatre in 2015, Mr. Rathore busted a quick dance move as he wended his way through the Toronto Raptors dance squad, which he'd hired for the occasion, arriving at the front of the stage as the music ended.

Mr. Rathore began selling investments in 1997, after attending York University. In 2002, he set up his own mutual fund sales firm under the sponsorship of a larger registered company, Independent Planning Group Inc. But the partnership didn't last long. Later that same year, IPG terminated Mr. Rathore after discovering he was operating another financial firm at the same time – a fact he hadn't disclosed, according to Canada's mutual fund regulator, the Mutual Fund Dealers Association of Canada (MFDA). Three years later, the MFDA slapped him with a lifetime ban from working in the sector because of the breach.

That other financial firm – which lay outside the grasp of the MFDA – was called Phoenix Pension Services, which Mr. Rathore launched in 2002 with Vince Petrozza, a fellow connoisseur of cars, couture and basketball. (He's now Fortress's chief operating officer and owns 20 per cent of the company; Mr. Rathore owns the other 80 per cent.) Phoenix and related company Phoenix Credit Risk Management helped clients unlock funds from registered retirement accounts – a process that includes applying to the federal government citing financial need – in order to repay personal debts. Many of its clients were vulnerable people referred there by collection agencies.

Vince Petrozza, chief operating officer of Fortress Real Developments, arrives at the company offices in Richmond Hill, Ont., in November of 2017.

CHRIS HELGREN

In 2007, Mr. Rathore and other Phoenix Credit Risk employees started to encourage their clients to use their unlocked retirement funds to buy shares in two tiny oil and gas companies that traded on the TSX Venture Exchange. Both penny stocks were controlled by B.C.-based investor Thalbinder Poonian, who paid Phoenix employees, including Mr. Rathore, large commissions for each referral – up to 28 per cent, in some cases.

Within two years, Phoenix clients had invested $16.5-million in the two companies, netting Mr. Rathore and his colleagues roughly $3-million in commissions. Unfortunately for investors, Mr. Poonian was running a market-manipulation scheme. When he and other insiders liquidated their positions in 2009, Phoenix clients were left holding worthless paper.

Mr. Poonian was eventually fined $10-million by the British Columbia Securities Commission. As for Mr. Petrozza and Mr. Rathore, they reached a voluntary settlement with the Ontario Securities Commission (OSC) in 2011 that stated Phoenix's clients didn't know anyone at the company was receiving a commission for referring them to Mr. Poonian's stocks. The statement also said Phoenix helped clients open brokerage accounts to make their purchases, and in many cases, those clients were told the share prices would rise. Neither Mr. Rathore nor Mr. Petrozza admitted any wrongdoing, but they agreed to pay an administrative penalty of $250,000 and "disgorge" a further $2.7-million, which was used to pay back victims of the scheme. Both men were also banned from working as registrants in the securities industry for 15 years.

There are parallels between Phoenix and their next business venture: Fortress Real Developments Inc.

The Fortress Real Developments office is seen in Richmond Hill, Ont., in September, 2017.

MARK BLINCH/GLOBE AND MAIL

Mr. Rathore and Mr. Petrozza spotted a gap in the real estate financing market a decade ago, while they were still recommending penny stocks via Phoenix. Developers, and condo builders in particular, have traditionally struggled to access early-stage financing – money to cover “soft costs” such as design and engineering work – from mainstream lenders. After all, the development business is risky; there’s always a chance a project will fail to get zoning approval or find buyers. That means the small number of private firms willing to lend to early-stage projects often charge high interest rates – well over 20 per cent annually.

Mr. Rathore and Mr. Petrozza had been promoting syndicated mortgages to wealthy investors – the traditional target for these products – since 2002, but they decided there was an even bigger untapped market among regular retail investors. These loans, typically provided by a pool of individuals, can be used for any type of real estate deal, including residential home purchases, but are often used to finance larger-scale property developments, including new condominiums.

Fortress’s role would be to match regular Canadians with the builders looking for early-stage financing. In their promotional materials, they called their approach “mainstreeting” and “mainstreaming” of syndicated mortgages. In a 2012 interview with real estate website BuzzBuzzHome.com, Mr. Rathore said Canadian real estate lending had never been available for direct investment by the general public, “so we saw a really interesting and exciting niche opportunity.”

Much like Phoenix, Fortress encouraged retail investors to tap into their RRSP savings, typically asking for a minimum syndicated mortgage investment of just $30,000. The low threshold prompted thousands of less wealthy investors – many of them targeted through ethnic radio stations, newspapers and websites – to jump aboard.

Fortress’s other key innovation was its commission structure. By law, only licensed mortgage brokers can sell syndicated mortgage products, and commissions typically range from 2 to 4 per cent. Fortress was offering an alluring 15 per cent. Word spread quickly among not just brokers, but also investment advisers and insurance agents, who would refer their clients to the brokers for a share of the commission.

“There were a lot of hungry people out there who jumped on that,” says Mitchell Wine, a Toronto lawyer who, along with Kevin Sherkin, has launched four class-action lawsuits against Fortress on behalf of investors in four projects.

Getting those investment advisers and insurance brokers on board was key to the success of Fortress’s fundraising, says Mr. Sherkin. Most ordinary investors would have balked had a stranger pitched them such an unfamiliar investment option. It worked because these mortgages were being recommended by advisers they knew and trusted.

“They preyed on people who had a tremendous amount of trust and were unsophisticated,” says Mr. Sherkin.

'My money is probably all gone': The people fretting over Fortress payments

Three investors in syndicated mortgages tell their stories.

Read the article

The heart of the operation was Fortress's in-house mortgage brokerage firm, initially known as Centro Mortgage and later renamed Building & Development Mortgages Canada Inc. (BDMC). It was located in the same building in Richmond Hill and owned by mortgage broker Ildina Galati. Mr. Petrozza and several other Fortress executives also worked as licensed brokers for BDMC, which means they were raising money from retail investors while also assisting the developers borrowing the funds. That's a potential conflict of interest: Ontario rules require mortgage brokers to tell investors about any relationships the brokerage firm has with all parties involved in a mortgage transaction and to disclose any conflicts.

To create more distance between investors and borrowers, BDMC began in 2011 to spin out three arm's-length brokerage firms (FDS Broker Services Inc., FFM Capital Inc. and FMP Mortgage Investments Inc.) that set up offices in strip malls around the Greater Toronto Area. In theory, they were independent firms, but most of the owners and principal brokers were former BDMC or Fortress employees who had set up the affiliates under the direction of Ms. Galati. An RCMP search warrant application filed in court in April said it appeared that two of the CEOs of the affiliate brokerages, Tony Amendola and Zafar Khawaja, also worked as vice-presidents at Fortress Real Capital, the company's investment arm. (Neither Mr. Amendola nor Mr. Khawaja responded to requests for comment.)

Bill Vasiliou, who oversaw regulation of Ontario's mortgage sector for 16 years as the province's registrar of mortgages, believes Fortress created the web of brokerages to give investors the impression they were offering independent advice about third-party Fortress deals.

"They set up non-arm's-length brokerages with their senior people as agents of those brokerages and straw individuals as principal brokers," says Mr. Vasiliou.

Fortress lawyer's, Mr. Fenton, disagrees, saying the brokerages were separate legal entities independent of the company.

Fortress's affiliated brokers advertised aggressively, highlighting the low-risk nature of syndicated mortgages and the 8-per-cent annual returns. They ran ads in ethnic newspapers and on ethnic radio stations, including promotions in Chinese and Portuguese. One affiliated broker distributed a brochure telling Fortress investors they could "invest like the bank," which Toronto lawyer David Franklin says gave the impression syndicated mortgages were just as safe as residential ones.

In reality, Fortress was selling low-ranking, pre-construction loans that were far less secure than your average home mortgage or even first-ranking construction loans typically offered by banks or other real estate financing firms.“You’re getting a second mortgage at a lower rate than the first mortgage, with no guarantees,” says Mr. Franklin, who is representing several aggrieved investors. “And yet, investors would go in because they didn’t understand that.” (Mr. Fenton counters that brokers were clear with investors about the riskiness of the loans.)

The affiliates held dozens of seminars and dinners across Canada each year, inviting potential investors, financial advisers and independent mortgage brokers to hear Mr. Rathore and other Fortress executives tout their projects. Many events featured pitches from developers like Mr. Lamb, whose Lamb Development Group has worked with Fortress on at least 12 projects. Mr. Lamb would not comment for this article, but at the black-tie Fortress Choice Awards in February, 2015, held at Toronto’s Liberty Grand, he told a huge crowd: “I’ve got to say that our little company would be nowhere today without Vince and Jawad helping us out.”

Advisers who referred a large number of clients to Fortress were invited to join Mr. Rathore at Toronto Raptors and Maple Leafs games at the Air Canada Centre, or flown on chartered planes to New York or Cleveland. At private events, he’d introduce them to sports stars like basketball great Steve Nash and NHLer Gary Leeman (a “brand ambassador” for one of the affiliate brokers). Toronto Blue Jays pitcher Marcus Stroman was hired as an inspirational speaker at a Fortress broker event in 2016.

The affiliate brokerages were enormously successful: BDMC raised about $800-million for developers between 2012 and early 2017 through the network. In 2016, affiliate FDS alone raised $68-million.

Not all mortgage brokers found the glitz alluring. Vincent Gaetano, who owns MonsterMortgage.ca Inc., steered clear of Fortress’s projects. The whole structure was unusual, he says, and the rich commissions should have been a warning to brokers, not a lure. “My red flag went up immediately – I was not interested,” says Mr. Gaetano. “My opinion is this is high-risk debt, and investors will eventually get slaughtered. I stay away from ‘too good to be true.’”

No one mentioned the high-risk nature of the Fortress investment to Mario Narciso and Fernanda Cortes. Everything they’d been told by their adviser and his mortgage-broker associate led them to believe they were being conservative with their money.

They were further reassured when, just as they were about to sign the documents – much of which the Portuguese-speaking couple didn’t understand – the broker suggested they speak to a lawyer who could give them “independent” advice on the deal.

Mario Narciso at his home in Vaughan, Ont., on Nov. 16, 2018.

CHRISTOPHER KATSAROV/GLOBE AND MAIL

When they dialed up the lawyer, the connection was poor (he told them he was driving on the highway), and Ms. Cortes says he spoke very fast. She didn't even catch his name. But not once did he mention any significant risks with the Fortress project, she says.

Four other investors who talked to *The Globe and Mail* also spoke to supposedly independent lawyers. What they didn't know was that some of those lawyers also worked for Fortress and were paid by the developers, creating potential conflicts of interest when it came to offering advice on the merits of the deals.

Derek Sorrenti, who runs his own law firm in Vaughan, north of Toronto, advised many Fortress investors. He has also acted often for Fortress in real estate transactions and was the trustee overseeing many of the syndicated mortgage loans. Mr. Sorrenti, who did not reply to requests to comment for this article, is named in several investor lawsuits filed against Fortress. The suits claim he failed to flag significant risks in the transactions and did not divulge his links to Fortress. Arlene McDowall, an investor who's suing both Fortress and Mr. Sorrenti, says that according to her investment documents, he was paid $2,500 for a 20-minute phone call with her.

Mr. Franklin says that in May, 2015, he filed a complaint with the Law Society of Ontario about the quality of legal work provided to many Fortress investors. But as of today, there are no regulatory proceedings against Mr. Sorrenti, according to the law society's website.

In October, 2017, however, the law society issued a bulletin, saying it had "become aware of instances" of investors sustaining significant losses on syndicated mortgages. It reminded lawyers of their obligation to avoid conflicts of interest and be "honest and candid with the client." Among the situations that would put a lawyer in breach of the rules would be representing a client investing in a syndicated mortgage while also having other interests in the same deal, the bulletin said.

Mr. Franklin says the guidance came too late to help most investors: "They believed the lawyers would tell them if there was any risk."

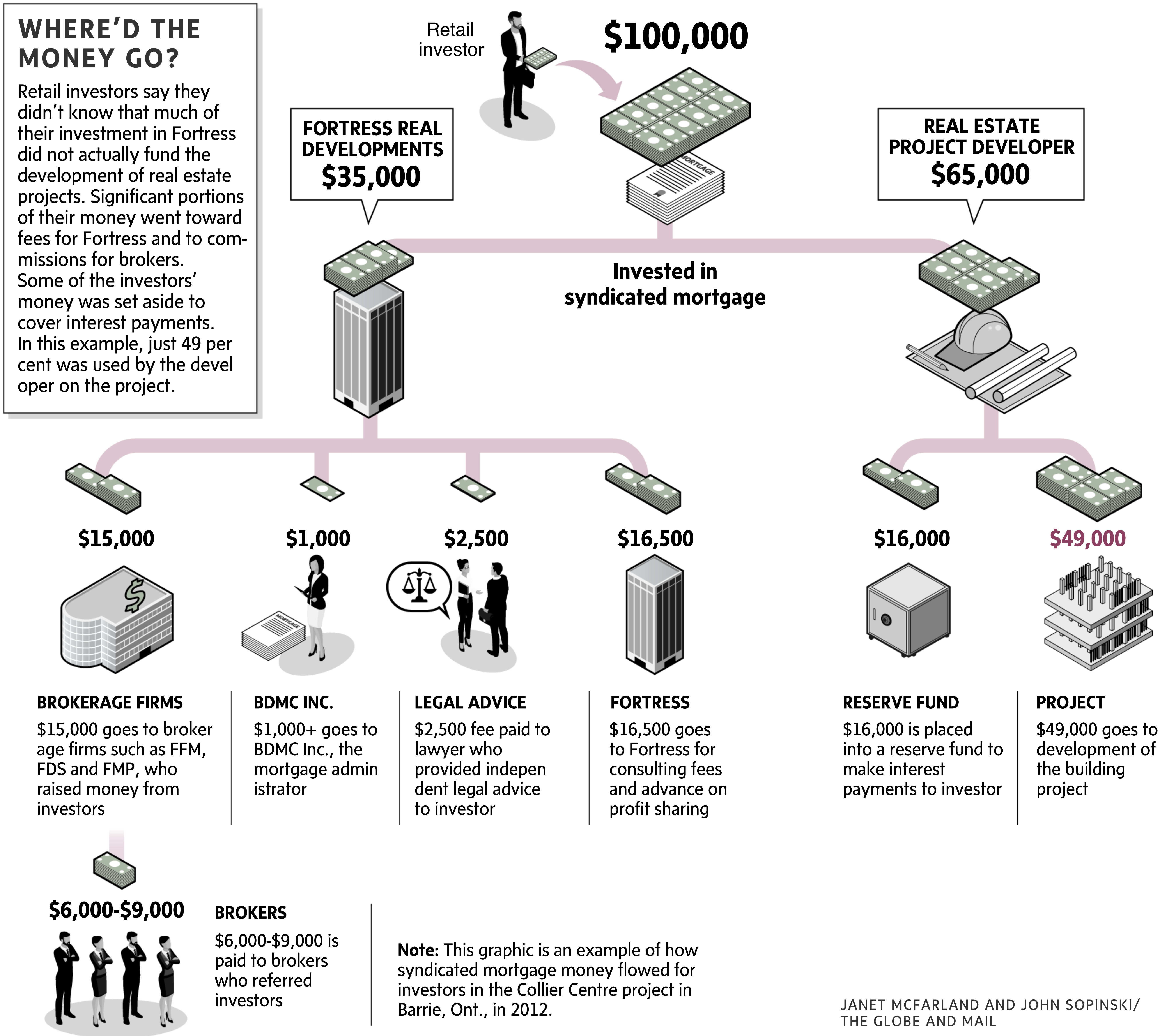
Investors – and even some external brokers – were also kept in the dark about management fees paid to Fortress. Investors said they were told there were none. At a seminar organized by one of Fortress's affiliated brokerages in 2016, Mr. Rathore stood on stage with the words "No Management Fees" projected on a white screen behind him.

But there *were* fees, and they were high.

Fortress typically took 35 per cent of the investments raised from syndicated lenders up front to pay fees and commissions, court filings show. Those included commissions for the brokers who sold the investments and a fee to BDMC for co-ordinating each loan.

Fortress also kept part of the money itself for consulting on the deals and was sometimes paid a share of the project's anticipated profits up front, even before the projects were built. For example, Fortress kept $5.9-million, or 35 per cent, of the $16.9-million provided by the first group of syndicated lenders on the Collier Centre project in 2012. The money went to pay fees to brokers, and included $2.28-million in payments to Fortress for co-development fees and profits, according to court filings.

In some syndicated deals, a further portion of the investment was also set aside by the developer to pay interest to the syndicated mortgage lenders. In other words, the interest being paid to investors came from their own money, rather than from the developer's cash reserves, a fact investors say they didn't know when they signed. On the Collier Centre deal, 16 per cent of investors' funds were set aside to make interest payments back to them. Combined with the 35 per cent that went to Fortress, less than 50 per cent of the money invested actually went toward developing the Barrie project.



JANET MCFARLAND AND JOHN SOPINSKI/ THE GLOBE AND MAIL

Mr. Fenton rejects investor complaints that they weren't told about Fortress's fees and commissions, saying mortgage brokers informed investors about the company's potential profit participation as required under mortgage regulations. Furthermore, he adds, all legal advice to investors came from reputable counsel "whose conduct has not, to Fortress's knowledge, ever been impugned."

Had investors known about the massive fees, however, Mr. Wine believes many of them would have backed away from Fortress deals. "They were told they were investing money to allow the developers to move forward with the projects," he says. "Why would they invest in something when one half of their money never got to the developers?"

No one else was able to warn investors. Fortress aggressively threatened or launched legal action against several people who commented or tweeted about the company, including Mr. Franklin and housing analyst Ben Rabidoux of boutique research firm North Cove Advisors. Fortress hit Mr. Rabidoux with a lawsuit in 2016 after he tweeted that he was concerned about risky syndicated mortgage loans. In one tweet, for example, he predicted the OSC would take control of syndicated mortgages and "slam the door" on "shadier operators." Mr. Rabidoux didn't mention Fortress by name, but the company's lawsuit claimed the context of his remarks made it clear the target was Fortress.

The lawsuit was finally dismissed in late August by the Ontario Court of Appeal. Mr. Rabidoux's lawyer, Gil Zvulony, says one of the saddest results of the long legal action is that it silenced those who could have warned investors. "If Ben had been allowed to speak freely – had he not been bullied into taking his tweets down – how many people would have seen that?" Mr. Zvulony asks. "Would they have thought twice about investing in these syndicated mortgages?"

As for the brokers, many were new to the industry, with little experience selling residential mortgages, let alone sophisticated financial products. According to a search warrant application filed in court as part of the RCMP investigation, one FDS broker who spoke to the police said he was coached to say the developer paid the fees and commissions from separate funds – not from investors' own money. He adds that "everyone" at affiliate brokerage FDS told him Fortress only got paid when a project was completed.

Another broker who began recommending Fortress mortgages to clients in 2011 says he knew nothing about how much the company was earning on each deal. The broker initially received a 6-per-cent commission on each investment, paid by one of Fortress's affiliated brokerage firms. Those commissions rose over time as he referred more clients – as high as 12 per cent of clients' funds.

He says he thought Fortress's syndicated mortgages were a great alternative to low-yielding bonds and GICs. "It was a way for clients to actually start making a reasonable rate of return," he says.

But two years in, he decided he didn't like the people he was working with and stopped recommending Fortress mortgages. Losing those fat commissions was "devastating" to his finances. "It was a hard thing to make a change, because you were being very well paid," he says. "And the market was still very robust." Fortress raised hundreds of millions of dollars after he stopped selling the products, he says.

Years later, some of his clients still haven't seen their loans repaid. "You feel very badly about that," he says. "Morally, if you care, you're so mad. It didn't have to be this way."

The commercial portion of Collier Centre in Barrie, Ont., on Nov. 13, 2018.

RYAN CARTER/THE GLOBE AND MAIL

Real estate developments often face unexpected delays before construction even starts, and Fortress's projects were no exception. Even in the company's early years, many dismayed retail investors received notices saying their projects were running behind. Some were told their promised monthly or quarterly interest payments would be suspended and instead accrue until the project was completed.

There was little they could do but wait, since their mortgage agreements required they extend the loans when requested. That meant investors couldn't seize the property when loans weren't paid on schedule, like traditional mortgage lenders can.

But Fortress soon had bigger problems. In late 2014, one of its most important development partners, Mady Development Corp., halted work on several major projects funded by Fortress syndicated mortgages, including Collier Centre, SkyCity and the Brookdale condo project in Toronto. Mady would later file for bankruptcy, and in 2015, Fortress took over its three biggest projects, promising to complete construction itself and repay investors. To that end, it raised an additional $36-million in syndicated loans for Collier Centre, including the $500,000 investment from Mario Narciso and Fernanda Cortes.

Meanwhile, the earliest group of syndicated investors were still owed nearly $16.9-million, a loan that ranked behind the $30-million owed to primary lender Laurentian Bank.

FIRST TO INVEST, LAST IN LINE

Regular investors funded syndicated mortgage loans for new development projects, including the Collier Centre in downtown Barrie, Ont. But as the troubled project raised more financing, new lenders got first priority on any prospective claims, and the syndicated mortgage loans were pushed down the priority list.

Mortgage loans registered on the property
Ranked in order of priority claim on the land, in millions of dollars

Rank	Lender	Amount of loans (**Total: $89.62-million**)
1ST	Morrison Financial Services	**$29.6** (33%)
2ND	Jaekel Capital	**$4** (4.5%)
3RD	Magnetic Capital Group	**$3.1** (3.5%)
4TH	**Second round of syndicated investors**	**$36** (40%)
5TH	**Original round of syndicated investors**	**$16.9** (19%)

JANET MCFARLAND AND JOHN SOPINSKI/THE GLOBE AND MAIL
SOURCE: FAAN MORTGAGE ADMINISTRATORS

But as it turns out, there simply wasn't enough value in the project to cover Laurentian (which ended up losing $6-million on the deal), let alone the syndicated investors.

The way Fortress valued its properties, in its efforts to persuade investors to hand over their money, has become a central issue in the RCMP's investigation.

In a search warrant application filed in April, investigators allege investors were given inflated land valuations for several Fortress projects, which persuaded them their mortgage loans would be safely cushioned by the real value of the property. For instance, Mady bought the Collier Centre land for $4-million, and the valuation used to back the Laurentian loan was $7-million. Yet, a syndicated mortgage disclosure statement given to investors and filed with FSCO in July, 2012 – mere weeks after Mady bought the property – pegged the “appraised 'as is’ value” at $21.8-million. The disclosure statement also noted that the $16.9-million syndicated mortgage, plus an earlier mortgage of $1.65-million, meant the total debt against the property would equal 85 per cent of the “as is” value. The math reassured investors that the loans were low-risk.

The $21.8-million figure came from an “opinion of market value” prepared by property valuators Cushman & Wakefield, which noted that it does not constitute a legal appraisal. The RCMP alleges in a search warrant application that it is improper to give investors an opinion of value and describe it as a current market value, and claims it has found similar valuation issues on other projects, including SkyCity in Winnipeg, Harmony Village Sheppard in Toronto and Crates Landing in Keswick, Ont.

However, Fortress lawyer Scott Fenton says investors were fully advised in writing of the assumptions and methodologies used by industry valuators to create “opinions of value” for the projects, Mr. Fenton said in a statement adding that the opinions of value clearly stated they were not appraisals.

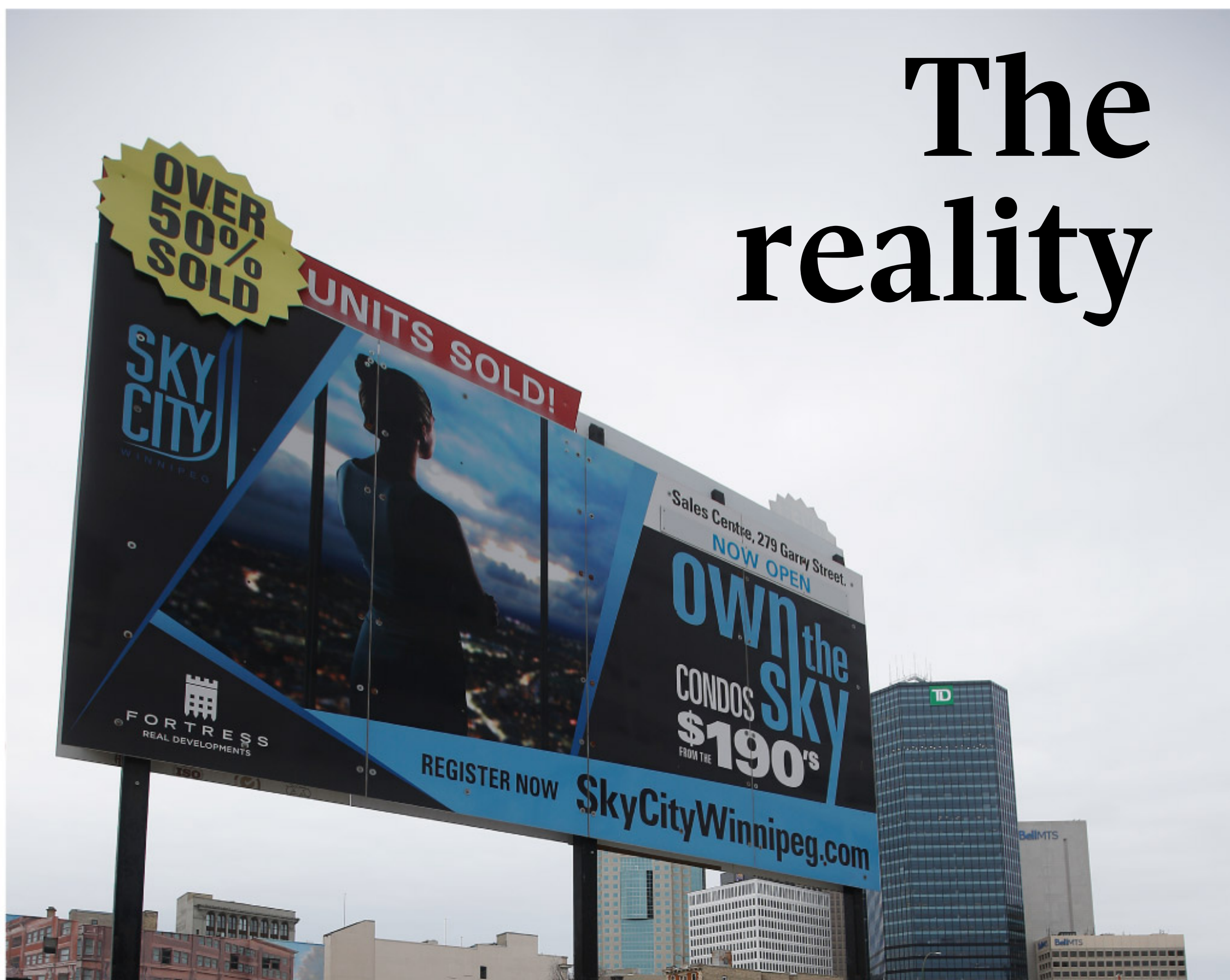
The valuation issue has also raised potential tax problems for investors, many of whom used RRSP funds to invest in Fortress’s syndicated mortgages. According to tax law, Canadians cannot hold a mortgage investment within an RRSP account when the value of the loan exceeds 100 per cent of the value of the property. As a result, the RCMP search warrant alleged mortgage brokers misled investors when they told them their loans were RRSP-eligible.

Mr. Fenton disagrees, saying Fortress got a legal opinion that each mortgage was RRSP-eligible. The RCMP, he says, is “relying on the musings of a police constable based on things he read on the Internet.”

As for the Collier Centre project, Fortress’s problems continue. With Fortress acting as developer, the residential tower was completed, but the office tower remains empty after tenants withdrew, and Fortress has applied to convert it into condos. Syndicated lenders, meanwhile, can only be repaid once the project is 100 per cent done.

Fortress also secured a new senior lender, Morrison Financial, when it took over Collier Centre in 2015. Morrison is currently owed $30-million in mortgage debt, and earlier this year, it filed notice that Fortress’s loan is in default. It has issued a notice of sale for the property and hired a real estate agent to look for buyers. The receiver controlling BDMC has warned the Collier sale could result in “significant losses” for syndicated investors, who rank behind Morrison.

Fortress has also been unable to complete the Brookdale project; it was put into receivership in June and sold in October and they have yet to disclose the sale price. As for SkyCity, it has seven mortgages registered on the land totaling $39-million and has been indefinitely postponed. Despite all the financing raised for the project, the site remains an undeveloped parking lot.




SkyCity was envisioned as the tallest building between Calgary and Toronto. The project has been indefinitely postponed, and the site remains a parking lot.
(Left: Fortress Real Developments brochure; right: John Woods/The Globe and Mail)

FSCO, the provincial body that regulates the mortgage industry, started receiving complaints – ultimately dozens of them – around 2011, according to a former FSCO employee who was granted anonymity by The Globe and Mail because the person was never authorized to speak about the investigations. Some of these grievances, which came from a mix of industry insiders, investors and anonymous sources, targeted Fortress itself; others pointed fingers at BDMC and its affiliated brokerage firms.

The former FSCO employee says many of the complaints were passed along to more senior staff for investigation, but nothing ever seemed to happen. In fact, the lack of action became a source of internal stress among front-line compliance staff. "These were serious complaints – there was ample evidence to move this forward to the investigations level," says the former staffer. "I found it very frustrating."

FSCO says it did conduct "a thorough and complex investigation into Fortress syndicated mortgages," according to an emailed statement. "Such investigations take time, and disciplinary actions must follow due process." The regulator also says it did not receive any consumer complaints about Fortress investments until 2014. But the former FSCO employee says there were earlier complaints about the sales practices of brokers selling the mortgages, if not necessarily about Fortress itself.

Nonetheless, the regulator didn't start a 60-day review of BDMC until the spring of 2017, which culminated in a voluntary settlement deal this past February.

To anyone unfamiliar with the Fortress structure, that agreement would be hard to understand. It outlines no allegations of wrongdoing. It simply lists a series of negotiated penalties for a group of brokerage firms whose relationship to one another is not explained. The deal also fails to explain why penalties were being levied in the first place and contains no admission of wrongdoing by any of the parties. BDMC lost its mortgage brokerage licence, as did Mr. Petrozza and the three principal brokers at BDMC's affiliated firms: Rosalie Spadafora, Michael Daramola and Glenn May-Anderson. (Mr. Rathore is not a registered mortgage broker.)

BDMC voluntarily agreed to be supervised by an independent mortgage management firm, FAAN Mortgage Administrators Inc., but FAAN soon ended up with complete control of the company after complaining that BDMC and Fortress weren't co-operating when it came to accessing information about outstanding mortgages. BDMC's three brokerage affiliates were allowed to keep operating, though two of them went out of business months later. The third, FFM – which was originally called Fortress Financial Management Inc. – recently shut down its website but is still licensed by the province.

As for Fortress, it wasn't part of the February settlement – FSCO said it has no authority over real estate developers. But in late August, the regulator notified Fortress that it was proposing to impose a $300,000 penalty against the company for violating the province's mortgage brokers act. (Mr. Fenton says Fortress asked for a hearing to challenge the penalty because it was "unilaterally imposed by

FSCO without a hearing or evidence.")

FSCO won't provide information about what Fortress is alleged to have done wrong, but says the public can attend a hearing before the Financial Services Tribunal. A date for that hearing has yet to be scheduled.

A model of the Collier Centre, and a temporary office in an unfinished commercial portion of the Collier Centre in Barrie, on Nov. 13, 2018.

RYAN CARTER/THE GLOBE AND MAIL

Since 2015, FSCO says it has taken enforcement action against 20 parties involved in various syndicated mortgage investments and has issued six warning notices on its website alerting consumers to the high risk of these investment products. It also says it has increased training and continuing education requirements for mortgage brokers selling them.

Coincidentally, in 2015, the Ontario government appointed an expert panel to review financial regulation in the province. The three-member panel found there has been inconsistent regulation, depending on the type of financial product being sold. The sale of securities, for instance, receives more oversight from the OSC than insurance or mortgage products do from FSCO.

"To the consumer or the investor, I think it comes as a great surprise that the products they thought looked and felt like ordinary securities products are all regulated in a different way, within a less robust regime," says panel member Larry Ritchie, a former vice-chair of the OSC. The panel recommended replacing FSCO with a new, independent regulator, called the Financial Services Regulatory Authority (FSRA), expected to launch in 2019. Mr. Ritchie has agreed to join the board.

The panel also recommended that oversight of syndicated mortgages shift to the OSC, which would bring Ontario in line with other provinces. Though no date has been set for the move, the OSC has published proposed new guidelines if or when the switch is flipped. The rules would allow syndicated mortgages to be sold to retail investors with an "offering memorandum," or OM – a stripped-down disclosure document that would have to include an official land appraisal and a clear risk assessment. Only exempt market dealers registered with the OSC would be allowed to sell them, and they would be required to do suitability assessments for each investor.

In the meantime, FSCO has announced its own reforms. As of July 1, 2018, investors in Ontario can't put more than $60,000 into most types of syndicated mortgages in any 12-month period unless they are "designated" investors with higher income and assets. And mortgage brokers must give investors written disclosure of the material risks of an investment, as well as an official land appraisal.

Critically, there is also a clearer requirement that mortgage brokers assess a client's objectives, risk tolerance and financial circumstances to ensure an investment is suitable for the investor. Mr. Ritchie believes there's still more to do, including rethinking how much training mortgage brokers should have before they're allowed to sell these products and whether they should be able to assess the investment in the broader context of an investor's overall financial plan, he says.

FSCO's spokesperson, Malon Edwards, says the regulator "will continue to do everything within our power to educate consumers about the risks of syndicated mortgages, to support the government's regulatory changes and make sure those licensed with us follow the rules."

Fortress problems

Troubled projects funded by syndicated mortgage loans arranged by Fortress. (Note: Dollar amounts are total value of all syndicated mortgage loans registered on the property. Do not include loans from senior lenders.)

Project: Brookdale, Toronto
Status: Seized by senior lender, sale of property approved in October
Amount of mortgage: $25.3-million

Project: Capital Pointe, Regina
Status: Construction ceased, borrowers plan to restart by next spring
Amount of mortgage: $33.3-million

Project: Collier Centre; Barrie, Ont.
Status: Senior lender has issued power of sale notice and has listed the property for sale
Amount of mortgage: $52.9-million

Project: Glens of Halton Hills; Georgetown, Ont.
Status: Filed insolvency notice as lenders moved to seize land, sale process under way
Amount of mortgage: $14.4-million

Project: Harmony Village Sheppard, Toronto
Status: Sold under receivership
Amount of mortgage: $31-million original amount, $19.5-million repaid

Project: Old Market Lane; Vaughan, Ont.
Status: Power of sale notice issued by lender in September
Amount of mortgage: $13.3-million

Project: SkyCity, Winnipeg
Status: Construction has halted and condo buyer deposits returned
Amount of mortgage: $32.2-million

Project: The Kemp; Barrie, Ont.
Status: Property up for sale, has conditionally sold several times but deals have not closed
Amount of mortgage: $18-million

Project: Triple Creek, Calgary
Status: Lenders have issued notice of sale, sale process not started yet
Amount of mortgage: $15.4-million

Project: Union Waterfront; St. Catharines, Ont.
Status: Senior lender put project into receivership, sale process launched
Amount of mortgage: $16.8-million

The RCMP had also been receiving complaints from distraught investors claiming they hadn't been repaid and were misled about the terms of Fortress projects. By April 13, 2018, officers in its Integrated Market Enforcement Team, which investigates major frauds, had secured warrants to search Fortress's head office, along with those of BDMC and its affiliates.

Fortress employees were just settling in for the day when a parade of RCMP vehicles, including one marked cruiser, pulled up in front of its building in an industrial park in Richmond Hill shortly after 9 a.m. A team of officers marched inside the low building, where they presented a search warrant, asked startled employees to leave, and set about photographing and searching each desk.

One senior employee, Charene Bunnett, challenged officers when they approached her office, asking to read the warrant before she was escorted out of the area. The RCMP was later granted a new search warrant to stop and search her car, telling a judge they had received an anonymous tip claiming she'd hidden a laptop and external hard drive before they'd managed to get to her office.

Ms. Bunnett's lawyer, Frank Addario, declined to comment on the RCMP's "untested" allegations.

Officers worked methodically through Fortress's building, focusing in particular on land valuation documents. Ultimately, they would spend three days inside the building, removing dozens of boxes of materials. At the same time, more than a dozen officers were searching five other Fortress-related sites.

Eight months later, the RCMP are still investigating Fortress and have laid no charges in the case. Investigators are only just starting to look at electronic documents and emails seized in the April search. (Before that process could begin, the Crown and counsel for Fortress had to agree on a protocol for the RCMP to review the material, which was then approved by a judge.)

Fortress, meanwhile, complains that everyone is focusing on its problems and ignoring its successes. It says syndicated mortgage investors have received payouts in 27 of about 80 projects, totaling $196-million in principal and $42.5-million in interest.

"Beyond any question, these statistics reflect a track record of considerable success by Fortress in a competitive industry," Mr. Fenton, Fortress's lawyer, said.

However, some investors only received partial payouts. The Harmony Village Sheppard condo project in Toronto, for instance, was never completed and was sold under receivership last year. Syndicated lenders, owed $31-million, were repaid $19.5-million from the proceeds after the receiver found a buyer for the land, according to receiver Brahm Rosen. He says syndicated investors should get another $1-million when the final funds are distributed. About $10.5-million in principal will not be repaid.

Another 10,000 investors are still waiting for news on how much of their money they'll get back. There are still almost 50 Fortress projects with outstanding syndicated mortgage loans worth more than $700-million. That total includes $560-million of loans now under the administration of FAAN and additional loans under the control of other trustees – primarily Mr. Sorrenti.

With all the company's recent legal problems, spooked lenders are calling loans and refusing to refinance. Many of the projects have been delayed for years, which means they could sell for little more than the vacant land value.

The company's long-stalled Union Waterfront project in St. Catharines was put into receivership in August, as was the similarly moribund Glens of Halton Hills project in Georgetown. And lenders have filed intentions to seize and sell at least 10 other projects. It's impossible to estimate how much investors could lose.

That has Fernanda Cortes and her husband deeply worried about their future.

Initially, the couple thought their investment was going well – they received two years of interest payments. But eventually, Fortress extended their loan, and the interest began to accrue. Then came news of the RCMP investigation, followed by numerous project defaults. The most worrying report came in October, when Ms. Cortes heard that Morrison Financial was taking control of the Collier Centre project and had hired a real estate agent to look for a buyer.

Troubled by the implications of the potential sale, she phoned her mortgage broker to ask what was happening. At first, she said, he denied that the site was under power of sale – the media was hyping fake news about the project. But he later acknowledged the property was under seizure and said there was little he could do to help.

The couple haven't seen a dime of their principal, and it's still unknown whether Morrison can raise enough money via a sale of Collier

Centre to pay back anything to lower-ranking syndicated investors.

“It seems hopeless because everyone is saying that nothing can be done,” says Ms. Cortes, who has launched an "Investors of Fortress Developments” Facebook page to share information with other Fortress investors. “I’m left in a nightmare I cannot wake up from.”

Although FSCO revoked BDMC’s mortgage brokerage licence in February, it allowed a new brokerage, Canadian Development Capital and Mortgage Services Inc. (CDCM), to set up in its place.

The provincial regulator maintains that CDCM is different from BDMC. While it also brokers syndicated mortgages for developers, the regulator says the new entity is not an administrator for those mortgages and doesn’t perform any services directly for investors. FSCO won’t comment on how much fundraising CDMC has done to date.

However, CDCM is based in the same building as Fortress (now stripped of all of the company’s signs and logos). And it is led by Julie Galati, the mother of Ildina Galati, who owned BDMC and surrendered her mortgage broker licence in February. The brokerage’s website states: “We close syndicated mortgages that fund real estate development projects in major city centres across Canada."

Editor’s note: An earlier version of this story stated that investigators are just starting to look at electronic documents and emails seized in the April search because of a legal challenge by Fortress’s lawyers. The story has been corrected to note that counsel for Fortress and the Crown in fact agreed on a protocol for the RCMP to examine the material, which was then approved by a judge.

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