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Re: Canadian Securities Administrators (“CSA”) Consultation Paper 91-401 on Over-the-Counter (“OTC”) Derivatives Regulation in Canada (the “Consultation Paper”)

The Canadian Bankers Association (“CBA”) works on behalf of 51 domestic chartered banks, foreign bank subsidiaries and foreign bank branches operating in Canada and their 263,400 employees to advocate for efficient and effective public policies governing banks and to promote an understanding of the banking industry and its importance to Canadians and the Canadian economy.

General

A large proportion of derivatives are carried out by banks in Canada which are federally regulated and, therefore, any prudential regulation of the banks associated with derivatives, should be deferred to the federal prudential regulators. Also, as banks carry out their derivatives activities globally, local securities regulation should not create barriers to the ability of the banks to continue their banking business on a global basis. Nevertheless, the CBA appreciates that the CSA must protect the integrity of marketplaces in Canada and the public investors or participants in those marketplaces. The CBA, therefore, appreciates the opportunity to provide comments on the Consultation Paper. In addition to general comments set out below, we have provided comments on some concerns we have with respect to the regulation of OTC derivatives in Canada, as well as our views on certain of the specific requests for comments outlined by the CSA.

Any OTC derivatives regulation will have a significant impact on our members, which are federally regulated in Canada. As has been discussed at the G-20 level, regulators in different countries should strive for cooperation and consistency with respect to the OTC derivatives regulation. We stress the need for uniform OTC derivatives regulation in Canada, across all provinces and at the federal level, as the key to any global action plan and Canada's ability to deliver on its G-20 commitments with respect to the OTC derivatives regulation. To encourage consistency and transparency, and to minimize costs and delays, the CBA recommends that the CSA proceed in collaboration with other derivatives initiatives in Canada, including the initiative by the Canadian OTC Derivatives Working Group¹, which is being implemented through collaboration with the Canadian Market Infrastructure Committee ("CMIC")². Specifically, it is recommended that any further work by the CSA with respect to clearing be consistent with CMIC's proposals in that regard, which are currently being developed. Lastly, it is important to ensure that sufficient time is allowed for implementation of any ultimate OTC derivatives regulation in Canada (for example, interoperability will certainly take time).

Capital

As noted by the CSA, Canadian banks are subject to capital requirements established by OSFI which are consistent with the requirements set out in the Basel II Accord and will soon have to be reconciled with the new Basel III requirements. While capital requirements may need to be reviewed to assess their adequacy to address the key risks relating to OTC derivatives, we are of the view that OSFI and the Investment Industry Regulatory Organization of Canada ("IIROC") would be in a better position to lead such an initiative as it pertains to Canadian banks and securities dealers, as the case may be. OSFI and IIROC have long been prudential regulators for Canadian banks and securities dealers, respectively, and have substantial experience in assessing adequacy of capital requirements for such entities.

¹ Canadian OTC Derivatives Working Group is an interagency group composed of members from the Office of the Superintendent of Financial Institutions ("OSFI"), the federal Department of Finance, the Ontario Securities Commission, l'Autorité des marchés financiers, the Alberta Securities Commission and the Bank of Canada (which is also the group's chair).

² CMIC is composed of major dealers and buy-side participants that are active in Canadian derivatives markets. It is a group with roots in the Industry Advisory Group comprising six of the largest Canadian banks which was created in January 2010 for the purposes of assessing international developments, collecting data on Canadian OTC derivatives markets and developing policy recommendations related to the implementation of G-20 commitments. Its area of focus includes standardization, clearing and trade reporting.

Clearing

The CBA recommends that the CSA work with CMIC on all clearing-related issues, especially given CMIC's current active involvement in the analysis of clearing options in the Canadian context. That being said, the CBA would like to offer the following general comments with respect to clearing.

The CBA endorses the CSA's recommended approach to implement mandatory clearing of OTC derivatives that are determined to be appropriate for clearing and capable of being cleared. Similar to the clearing exemptions found in the proposed rules internationally, exemptive relief should be made available to non-financial corporate counterparties whose derivatives trades are primarily for hedging purposes or do not exceed a specified threshold (individually or aggregate volume over a time period which takes into account off-setting transactions), as such activities do not contribute to systemic risk.

Given that a large portion of derivatives activity by Canadian financial institutions (except equity-linked) occurs with foreign counterparties, coupled with the need to harmonize the Canadian derivatives regulatory regime with international jurisdictions, the evaluation criteria used to identify OTC derivatives eligible for clearing should be broadly consistent with criteria applied, or proposed to be applied, under similar international legislation, including: (i) the reduction of systemic risk; (ii) the liquidity of contracts; (iii) the availability of pricing/valuation information; (iv) the ability of at least one central counterparty clearing house (a "CCP") to handle the volume of contracts; (v) the level of client protection provided by the CCP; and (vi) the clearing costs.

In addition, while perhaps premature given the infancy of this legislative initiative, we note that the Consultation Paper does not address how the clearing obligation, when it becomes effective, would impact pre-existing derivative contracts. Under the United States *Dodd-Frank Wall Street Reform and Consumer Protection Act*, such contracts are exempt from clearing if reported to a repository within six months from the effective date of the legislation.

Electronic Trading

The CSA notes in the Consultation Paper that further study, in collaboration with market participants, will be necessary to determine the eventual scope of a regulatory mandate for electronic trading. We agree with the CSA that there are many valid reasons why OTC derivatives products trade separately from exchange markets (e.g., many end users often want to have the ability to hedge very specific risks; lower trading costs; increased flexibility), and that much can be achieved through post-trade transparency utilizing data gathered by trade repositories and central clearing. We also wish to point out that changes to the OTC derivatives market resulting from G-20 commitments will arguably result in an increased interest in processing derivatives transactions more efficiently and that increased electronic trading of OTC derivatives is likely an inevitable outcome of the current efforts aimed at standardization, clearing and trade reporting of OTC derivatives. It is therefore premature for the CSA to regulate electronic trading of OTC derivatives. For these reasons, we believe that mandating electronic trading of OTC derivatives would be both too restrictive and unnecessary.

Trade Repositories

Similar to the point made about the desirability of consultation with CMIC on all clearing-related issues, the CBA recommends that the CSA work with CMIC on all issues related to trade reporting. Subject to the foregoing, we would like to offer the following general comments with respect to trade repositories.

Mandatory reporting of all OTC derivative trades to a trade repository, whether Canadian or global, should ensure that Canadian regulators have access to transaction data involving all Canadian financial institutions, regardless of where the trade is booked or cleared. It would also seem pragmatic from a technological perspective that the reporting obligation could be fulfilled by a CCP for cleared trades, if feasible. In addition, we want to stress the need to ensure that duplication of reporting is avoided and a mechanism is in place to ensure modifications and terminations of contracts are properly reported.

Given that the protection of data received and disseminated by trade repositories is vital, the establishment of a Canadian trade repository could potentially mitigate any security related concerns and provide easier access to local regulators.

In addition, publication of individual counterparty positions, even historical, is tantamount to disclosing trading strategies and may deter some participants from trading in the first place. As such, we submit that only very generic aggregated data, such as price information, should be made publicly available on a historical basis.

We look forward to working with the CSA, through CMIC and otherwise, on issues arising from the creation and use of trade repositories, including the ownership of the data in the repository, risks involved in the sharing of data, royalties for the use of data, etc.

End-User Exemptions

Similar to the exemptions found in the proposed rules internationally, we are of the view that exemptions from the mandatory clearing (as discussed above), electronic trading, margin and collateral requirements should be made available to non-financial corporate counterparties whose derivatives trades are primarily for hedging purposes or do not exceed a specified threshold (individually or aggregate volume over a time period which takes into account off-setting transactions), as such activities do not contribute to systemic risk.

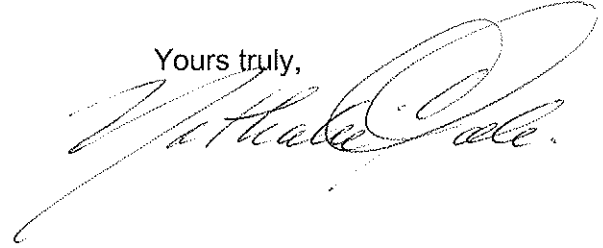
Enforcement and Surveillance

In addition to the jurisdictional issue (as discussed above), which is particularly relevant in the context of surveillance and enforcement, some of our members query the need for a surveillance and enforcement system for OTC derivatives, at least in the initial stages of the development of an OTC derivatives framework in Canada. If there are market abuses that the CSA is particularly concerned about, it is not clear from the Consultation Paper what those concerns might be and how the giving of jurisdiction to the CSA members to support market surveillance and enforcement activities will address the concerns that the CSA may have.

If and when such system is established, we are of the view that a centralized approach to the surveillance of the Canadian OTC derivatives market would be ideal, on account of the flood of information requiring analysis by regulators. If provincial regulators are granted surveillance authority, it is crucial they are equipped with the necessary resources and expertise to ensure surveillance/enforcement is robust and consistent across all provinces in order to mitigate the perception of regulatory arbitrage within Canada. This, in our view, would increase the chances of consistent regulatory interpretation, application and enforcement, and ultimately result in an increased compliance and market certainty.

The CBA appreciates the opportunity to express our views regarding the proposed OTC derivatives regulation in Canada, as discussed in Consultation Paper. We would be pleased to answer any questions that you may have about our comments.

Yours truly,

A handwritten signature in black ink, appearing to read "J. Michael Cole". The signature is written in a cursive style with a large, looping initial "J" and a long, sweeping underline that extends to the left.