



**Canadian Life
and Health Insurance
Association Inc.**

**Association canadienne
des compagnies d'assurances
de personnes inc.**

September 17, 2012

John Stevenson, Secretary
Ontario Securities Commission
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Me Anne-Marie Beaudoin
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Dear Sir/Madam:

**Canadian Securities Administrators' Consultation Paper 91-406 on Derivatives:
Central Counterparty Clearing**

The Canadian Life and Health Insurance Association is pleased to provide comments on the Canadian Securities Administrators' Consultation Paper 91-406 on Derivatives: OTC Central Counterparty Clearing ("CP 91-406").

Established in 1894, the Canadian Life and Health Insurance Association (CLHIA) is a voluntary trade association that represents the collective interests of its member life and health insurance companies. The industry, which provides employment to almost 135,000 Canadians and has investments in Canada of \$514 billion, protects more than 26 million Canadians through products such as life insurance, annuities, RRSPs, disability insurance and supplementary health plans. It pays benefits of almost \$65 billion a year to

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Canadians and administers over one-half of Canada's pension plans. Canadian life insurance companies participate as end-users in Canadian and foreign derivatives markets.

The CLHIA is generally in agreement with the CSA's proposed framework for centralized clearing in the Canadian OTC derivatives markets. The introduction of requirements for central counterparty (CCP) clearing of previously bilaterally cleared or uncleared derivatives transactions will enhance the transparency of markets and enhance the overall mitigation of risks.

The CLHIA is pleased that the Committee is working with foreign regulators to develop international standards. The CLHIA agrees that the Canadian OTC derivatives market comprises a relatively small share of the global market and that it is crucial that rules be developed for the Canadian market that accord with international practice to ensure that Canadian market participants have full access to international markets. Given the small size of the Canadian market, the CLHIA urges Canadian regulators to observe the developments in other principal jurisdictions such as the United States and Europe. Canada should not be implementing new requirements on a stand alone basis and should not be proceeding faster than the other principal jurisdictions such as the United States and Europe. As noted in our response to question 11 below, uniformity among Canadian jurisdictions also remains imperative. Barriers must not be created by having differing requirements in one jurisdiction or compared to the others.

We have the following specific comments related to various issues raised in the paper.

Backloading of pre-existing transactions

The CLHIA agrees that the back-loading of pre-existing transactions should be done on a voluntary basis. Valuation of pre-existing transactions will present challenges, and a methodology or protocol with respect to such valuations will need to be developed, consistent with approaches taken by clearing counterparties internationally.

Question 2. For which asset classes do you consider CCP clearing is inappropriate or not currently feasible based on the factors described herein, and for what reasons?

The industry expects that initially, only a small percentage of the OTC derivatives transactions currently being undertaken will be able to be electronically cleared. The industry agrees that expanded electronic clearing should proceed as soon as technologically possible as it promotes the benefits of increased price discovery and transparency in the market.



Question 3. What are the costs and risks involved in moving particular derivatives or classes of derivatives transactions to CCP clearing that regulators should consider in determining if a derivative should be subject to a CCP clearing requirement?

The cost of a derivative transaction relates primarily to the cost of initial margin. If the list of financial instruments eligible to be used for margin is too narrow, then it will result in transactions becoming more costly. The industry understands that a CCP requires highly liquid and transparent assets to meet its operational requirements. However, from the life insurance industry point of view, a broad range of assets needs to be acceptable recognizing the types of assets which insurers hold and to allow for flexibility. Less liquid assets should be acceptable to satisfy margin requirements with an appropriate reduction of value.

Question 4. Does a deferred submission, be it measured in minutes, hours or days, engender significant counterparty or other risks that would make the imposition of a strict timeframe for submission to a CCP, and the acceptance by the CCP necessary?

Generally speaking, the faster the reporting the better. Real time reporting aids with price discovery and assists with creating an efficient market. For very large trades, if the market becomes aware of the transaction, this will tend to have the effect of increasing the price. It is appropriate to allow a deferred submission for large trades within a reasonable timeframe.

Question 5. The Committee asks whether an exemption from mandatory CCP clearing for intra-group transactions is appropriate, including a description of the risks that they could pose to the marketplace and the costs of migrating such transactions to a CCP.

The life insurance industry strongly recommends an exemption from mandatory CCP clearing for intra-group transactions. Insurers often arrange OTC transactions with an arm's length entity (e.g., a bank) and then do an internal swap with an affiliate for cash or collateral management or other internal reasons. Trade reporting and clearing with respect to such transactions would not result in greater transparency; to the contrary, it would result in duplication and distortion of the numbers of true market transactions. Imposing collateral requirements on inter-affiliate transactions would have an impact on the liquidity of the participants and constitute a significant burden. It's unclear what risks would be addressed by imposing such constraints on inter-affiliate transactions.



Question 6. Is it appropriate to ensure that Canadian market participants have meaningful input into operational decisions of a CCP operating in Canada?

It is appropriate that Canadian market participants have input into the operational decisions of a Canadian-based CCP. A regulatory framework should be established consistent with that of other jurisdictions. The imposition of more stringent operating or corporate governance requirements on a CCP which operates in multiple jurisdictions would constitute a barrier to a CCP considering operations in Canada.

Question 7. Do the Committee's proposals relating to corporate governance of a CCP address potential issues relating to conflicts of interest that may arise in the operation of a CCP? If not, what other measures would address such conflicts of interest?

The CLHIA generally agrees with the proposed governance model for a Canadian-based CCP, including independent board members and an advisory committee to allow stakeholder input into operational decisions, to the extent that the model is consistent with that used in other jurisdictions.

It should be noted that if a CCP is owned by a Canadian financial institution this may create a natural conflict of interest. In this regard, it would be appropriate to establish rules regarding the ownership of a CCP.

Question 8. The Committee seeks public comment on the relevance of developing rules allowing for access to CCPs regardless of trading venue. Is this of concern in the Canadian marketplace at this time or in the future?

A CCP should be neutral to what platform trading takes place on. It should be possible for participants to mix and match platforms and brokers as market participants wish to.

Question 10. Generally, the Committee has endeavoured to follow international recommendations in the development of the recommendations for Canada in this paper. Are there recommendations that are inappropriate for the Canadian market?

The life insurance industry believes that Canada should be more flexible about what constitutes eligible collateral than has been the practice in the United States and in Europe. The tendency in the United States and Europe has been to impose higher capital requirements when trades are not electronically cleared. If technology is not available to clear, participants should not be penalized by imposing higher margin requirements.



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Question 11. Are there changes to the existing regulatory framework that would be desirable to accommodate a move to CCP clearing?

A totally uniform approach among all Canadian jurisdictions is critical to the efficient operation of the derivatives marketplace. The enactment of legislation and rules by each CSA jurisdiction is likely to lead to inconsistencies. The imposition of registration and reporting requirements by the various CSA jurisdictions will be burdensome for CCPs. Legislation accommodating the ability to develop one national regulatory framework should be considered. This approach would enable Canada to enter into cooperative arrangements with other jurisdictions in accordance with the FMI Principles.

The CLHIA appreciates the opportunity to provide its comments on the Consultation Paper. If you require any additional information at this time, please feel free to contact me by e-mail at JWood@clhia.ca or by telephone at 416-359-2025.

Yours truly,

James Wood
Counsel