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June 17, 2013

Re: Canadian Securities Administrators ("CSA") Staff Consultation Paper 91-407 Derivatives: Registration (the "Consultation Paper")

INTRODUCTION

The Canadian Market Infrastructure Committee ("CMIC") welcomes the opportunity to comment on the Consultation Paper dated April 18, 2013 published by the Canadian Securities Administrators OTC Derivatives Committee (the "Committee") relating to the proposal for the regulation of key OTC derivatives market participants through the implementation of a registration regime.

CMIC was established in 2010 to represent the consolidated views of certain Canadian market participants on proposed regulatory changes. The membership of CMIC consists of the following: Bank of America Merrill Lynch, Bank of Montreal, Caisse de dépôt et placement du Québec, Canada Pension Plan Investment Board, Canadian Imperial Bank of Commerce, Deutsche Bank A.G., Canada Branch, Healthcare of Ontario Pension Plan, HSBC Bank Canada, JPMorgan Chase Bank, N.A., Toronto Branch, Manulife Financial Corporation, National Bank of Canada, OMERS Administration Corporation, Ontario Teachers' Pension Plan Board, Royal Bank of Canada, The Bank of Nova Scotia and The Toronto-Dominion Bank.

CMIC brings a unique voice to the dialogue regarding the appropriate framework for regulating the Canadian OTC derivatives market. The membership of CMIC has been intentionally designed to present the views of both the 'buy' side and the 'sell' side of the Canadian OTC derivatives market, as well as both domestic and foreign owned banks operating in Canada.

OTC derivatives are an important product class used by both financial intermediaries and commercial end-users to manage risk and exposure. Systemic risk oversight of the OTC derivatives markets is an

essential component of the long term financial stability and growth of Canadian financial markets and their participants.

CMIC appreciates the consultative approach being taken by the CSA in considering the proposed registration regime. CMIC believes that this approach will lay the foundation for the development of a Canadian regulatory structure[1] that will satisfy Canada's G-20 commitments by addressing systemic risk concerns in OTC derivatives markets.

Limit on Scope of this CMIC Letter

The Consultation Paper is focussed on the registration of various categories of OTC derivatives market participants. CMIC is not an advocacy group for its members and it is beyond CMIC's mandate to represent or provide commentary to the CSA on the form, if any, of OTC derivative registration regime (and any associated jurisdictional issues) for each category of market participant that is represented within CMIC. As such, this letter will not address the jurisdictional issues raised by the Consultation Paper. Instead, some CMIC members through their respective industry associations may address in separate letters to the CSA the issues raised by this Consultation Paper in relation to their respective regulatory circumstances and jurisdictions. In addition, individual CMIC members may also make separate submissions to the CSA in relation to OTC derivative registration issues based on their unique regulatory circumstances. As it has in all of its submissions, this letter will reflect the consensus of views within CMIC's membership about the proper Canadian regulatory regime for the OTC derivatives market.

OVERVIEW

CMIC supports the regulatory progress that has been made internationally towards meeting the G-20 commitments and we encourage the CSA to continue to work closely with its global counterparts and other international bodies towards the common goal of meeting the G-20 commitments. In this regard, CMIC has consistently supported in its various submissions to the CSA the introduction of a reporting and clearing regime for OTC derivatives. However, the Consultation Paper introduces very significant additional requirements that are outside the G-20 commitments. The development of a registration regime for the regulation of OTC derivatives market participants is not part of the G-20 commitments. The G-20 commitments can be met without a specific registration requirement, as evidenced by the approach taken in Europe,[2] and we urge the CSA to give serious consideration to an OTC derivatives regulatory regime in Canada that does not require registration. In particular, CMIC's strong recommendation is that the CSA should give serious consideration to deferring the decision on whether to implement a registration regime until after a period of two years of trade reporting data is available.

Aside from the fact that a registration regime is not required to meet the G-20 commitments, CMIC submits that a broad-based and burdensome registration regime is unnecessary in purely regulatory terms. We are not aware of any meaningful degree of market misconduct or mischief in the Canadian OTC derivatives market that such registration regime could be intended to address. Further, no evidence has been presented that the imposition of the registration requirements set out in the

[1] References to "regulation" or "regulators" within this document will be considered to include market, prudential and systemic risk regulators.

[2] While the European Union Markets in Financial Instruments Directive ("MiFiD") recognizes "investment firms" as registrants, which term captures certain OTC derivatives market participants, additional or duplicative registration requirements have not been imposed in connection with the EU approach to meeting its G-20 commitments. Further, certain entities, such as banks, insurance companies and pension funds, are exempt from the application of MiFiD in whole or in part. We note that such categories of exempt entities represent a large proportion of Canadian OTC derivatives market participants.

Consultation Paper will provide a benefit to the Canadian OTC derivatives market, or to Canadian regulators, which is material enough to outweigh the costs and sizable risks. This is of particular concern where it can be predicted, as noted below, that imposing a rigid registration regime in a relatively smaller market such as Canada could significantly impair liquidity – market participants (particularly from outside Canada) may choose to withdraw from the market. Given that the Consultation Paper is outside the G-20 systemic risk objectives of OTC derivatives reform, we strongly urge the CSA to defer the decision on whether to implement an all encompassing registration regime.

In our responses (the "CMIC TR Letter", the "CMIC S&E Letter", the "CMIC S&P Letter", the "CMIC End-User Letter", the "CMIC CCP Letter" and the "CMIC Model Scope and TR Rules Letter", respectively, and collectively, the "CMIC Letters")[3] to the consultation papers issued by the CSA relating to OTC derivatives trade repositories (the "TR Paper"),[4] surveillance and enforcement of the OTC derivatives market (the "S&E Paper"),[5] segregation and portability in OTC derivatives clearing (the "S&P Paper"),[6] the exemption of end-users of OTC derivatives from certain proposed regulatory requirements (the "End-User Paper")[7], central counterparty clearing (the "CCP Paper")[8] and model provincial rules for derivatives product determination and trade repositories and derivatives data reporting (the "Model Scope and TR Rules Paper")[9] we emphasized that a Canadian regulatory framework for OTC derivatives must be harmonized and streamlined to the greatest extent possible across the provinces and territories and with federal authority over systemic risk. We also emphasized the need for rules that are aligned with global standards having due regard for the unique Canadian legal and market characteristics. A related point raised in the CMIC Letters was that, because of Canada's relative position in the global market, any imposition of regulatory hurdles on OTC derivatives market participants that are unique to Canada could pose a serious risk of placing Canadian participants at a disadvantage by impeding their access to global markets. The CMIC

[3] Response of CMIC dated September 9, 2011 to the TR Paper. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20110909_91-402_cmic.pdf. Response of CMIC dated January 25, 2012 to the S&E Paper. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20120125_91-403_cmic.pdf. Response of CMIC dated April 10, 2012 to the S&P Paper. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20120410_91-404_cmic.pdf. Response of CMIC dated June 15, 2012 to the End-User Paper. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20120615_91-405_cmic.pdf. Response of CMIC dated September 21, 2012 to the CCP Paper. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20120921_91-406_cmic.pdf. Response of CMIC dated February 4, 2013 to the Model Scope and TR Rules Paper. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20130204_91-301_cmic.pdf.

[4] CSA Consultation Paper 91-402 – Derivatives: Trade Repositories dated June 23, 2011. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20110623_91-402_trade-repositories.pdf.

[5] CSA Consultation Paper 91-403 – Derivatives: Surveillance and Enforcement dated November 25, 2011. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20111125_91-403_cp-derivatives.pdf.

[6] CSA Consultation Paper 91-404 – Derivatives: Segregation and Portability in OTC Derivatives Clearing dated February 10, 2012. Available at http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20120210_91-404_segregation-portability.pdf.

[7] CSA Consultation Paper 91-405 – Derivatives: End-User Exemption dated April 13, 2012. Available at: http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20120420_91-405_end-user-exemption.pdf.

[8] CSA Consultation Paper 91-406 - Derivatives: OTC Central Counterparty Clearing dated June 20, 2012. Available at: http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20120620_91-406_counterparty-clearing.pdf.

[9] CSA Consultation Paper 91-301 – Model Provincial Rules - Derivatives: Product Determination and Trade Repositories and Derivatives Data Reporting dated December 6, 2012. Available at: http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20121206_91-301_model-provincial-rules.pdf.

Letters also recommended that additional information and clarity is needed before a comprehensive regulatory regime for OTC derivatives can be developed.

Consistent with our positions advanced in the CMIC Letters, we submit that the key themes to be considered at the outset of the development of a regulatory regime for OTC derivatives are harmonization, both across Canada and with international jurisdictions, impact on Canadian market participants and available information. Each of these themes is discussed in more detail below, following which are specific responses to the questions posed in the Consultation Paper.

Harmonization

In the CMIC Letters, we have advocated that Canadian regulation of OTC derivatives should be harmonized as much as possible with international regulations. The Canadian market is different from the larger international OTC derivatives markets, both in number and composition of market participants, particularly as compared with the United States. As mentioned above, registration is not a G-20 commitment and it is CMIC's view that, for this smaller Canadian market, this is one area in which Canadian regulations should not be harmonized[10] with the United States under the Title VII of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* ("Dodd-Frank") but instead, Canada should follow the European approach (as discussed in more detail below under "General Comments"). In fact, we do not believe any of the smaller foreign OTC derivatives markets is mandating or contemplating a fulsome registration regime such as the one set out in the Consultation Paper.

As it relates to harmonization within Canada, in developing the Canadian regime for the regulation of OTC derivatives market participants, Canadian regulators should be alert to the risk of imposing duplicative or contradictory requirements. Such a risk is relevant in a number of contexts, including the imposition of redundant or inconsistent requirements across provinces and territories, but also extends to the potential for conflict with or duplication of existing domestic prudential regulation. While CMIC recognizes the importance of ensuring that any gaps in the regulatory framework are adequately addressed, we submit that it is equally important to ensure that overlap and duplication is avoided to the greatest extent possible. In this regard, consideration should be given to passporting and/or equivalency regimes both within Canada and, where applicable, with international regulators. We submit further that in order to avoid duplication of efforts and the potential for inconsistent application, any passporting or equivalency determinations should be made as between the applicable regulators and should not require individual participants to apply for such treatment. For example: (i) Canadian participants that are required to register should be permitted to deal only with their respective primary securities regulator (similar to the existing rules for securities registrants), and (ii) blanket equivalency determinations should be made both for Canadian participants subject to appropriate regulation within Canada (i.e. participants that are registered under the dealer category of Canadian securities laws, or those that are subject to regulation by certain prudential regulators) and for international participants subject to specified international regulatory regimes.

Impact on Canadian Participants

Prior to imposing any registration requirements, we urge the CSA to consider the potential impact of such requirements on the Canadian OTC derivatives market and its participants. Given the global nature of the OTC derivatives market and Canada's relatively small size within that market, Canadian participants routinely transact with international counterparties. In fact, our best available data indicates that over half of the trading in Canadian-dollar interest rate products involves at least one

[10] Though, of course, it is CMIC's view that Canadian regulations should not be *inconsistent* with international regulations.

party that is not a resident of Canada[11] and over 78% of OTC derivatives of the largest Canadian banks are with counterparties outside of Canada.[12] Maintaining ongoing access to this liquidity is of critical importance to the proper functioning of markets. Canada's relative position within the market also makes it difficult for it to impose additional or unique regulatory requirements without creating barriers to access for market participants. If the proposed Canadian regime has extra-territorial effects, international market participants may determine that it is too burdensome to comply with the Canadian requirements and choose to avoid transactions with Canadian counterparties. CMIC stresses the importance of OTC derivatives trading as a tool for the mitigation of systemic risk and wishes to emphasize that the Canadian regulatory regime should not impede the ability of Canadian market participants to access global markets. Any such impediments would disadvantage Canadian participants and have a very material adverse effect on liquidity in the Canadian marketplace (thereby potentially increasing systemic risk).

Critical Information Should be Assembled

As noted in the CMIC End-User Letter, CMIC supports a broad, principles-based exemption framework that encourages end-users to participate in the OTC derivatives market rather than a series of bright-line tests and specified criteria. We wish to reiterate this position in relation to the proposed registration regime while also emphasizing the need for clarity in the establishment of such principles. Further clarity is also required with respect to the key definitions used throughout the Consultation Paper, such as (but not limited to) "derivatives" and "Large Derivative Participant". It is unclear to us at this time which products and participants are meant to be captured by the proposed registration regime. CMIC encourages the CSA to take the time required to study trade repository data as it becomes available prior to the development of any registration regime in Canada. Only with such information will it be possible to determine the appropriate balance between regulation and access to markets. Further, the recommendations set out in the Consultation Paper would, if implemented, place a very high administrative and operational burden, not only on market participants, but also on the members of the CSA. In our view, we do not believe that the regulatory infrastructure to deal with all the requirements set out in the Consultation Paper currently exists, and to put such infrastructure in place would be extremely onerous and costly. Therefore, we strongly recommend a study of at least two years of data from trade repositories to identify any regulatory gaps or concerns before deciding whether to institute a registration regime in Canada in respect of the OTC derivatives market.

SPECIFIC RESPONSES TO CONSULTATION PAPER QUESTIONS

General Comments

As noted above, the Canadian OTC derivatives market is different than the US market. It is a much smaller, less liquid market, with a large majority of transactions entered into with non-domestic participants. As mentioned above, our information supports the view that over half of the trading in Canadian-dollar interest rate products involves at least one party that is not a resident of Canada.[13] Further, the aggregate notional amount of OTC derivatives transactions entered into by the 6 largest

[11] "Curbing Contagion: Options and Challenges for Building More Robust Financial Market Infrastructure" Remarks by Tim Lane, Deputy Governor of the Bank of Canada, Society for Worldwide Interbank Financial Telecommunication, Annual Sibos Conference, Toronto, September 19, 2011.

[12] In 2010, 78% of over-the-counter derivatives of the largest Canadian banks are with counterparties outside of Canada. Source: "Reform of Over-the-Counter (OTC) Derivatives markets in Canada: Discussion Paper from the Canadian OTC Derivatives Working Group", October 26, 2010, page 23 available at: http://www.bankofcanada.ca/wp-content/uploads/2010/10/reform.pdf.

[13] *Supra* note 11.

Canadian banks represent 3% of global OTC derivatives transactions.[14] Accordingly, any regulatory regime proposed by the Committee must be evaluated in the context of the specific characteristics of the Canadian market. If the regime imposes requirements which are too onerous, and is one in which costs outweigh benefits, non-domestic participants may well choose to avoid entering into OTC derivatives with Canadian market participants, thus reducing liquidity in Canada. We have seen this occur in the US where certain non-US banks have stopped trading with US entities in order to avoid registration in the US.[15] If foreign banks take these extreme measures with regard to the US market, which is a much larger market than Canada, it is reasonable to assume that some foreign banks might well take the same position in relation to the Canadian market, particularly if registration is required with multiple Canadian regulators. At a minimum, if non-domestic dealers are required to register, even if they are exempt from a majority of the requirements for registered dealers, market participants may well be motivated to move their OTC derivatives transactions offshore.

CMIC proposes that following a US-type approach to registration therefore is not appropriate in Canada and that MiFID is a more appropriate approach for the Canadian market. CMIC submits that a more useful and effective approach for the Canadian market would be to impose minimum business conduct requirements on all professional derivatives counterparties ("Professional Parties") which would capture all parties that are in the business of (a) making OTC derivatives markets, (b) as specified in the manner below, trading in, or intermediating, OTC derivatives for a fee or for profit, or (c) advising in OTC derivatives.

We provide greater clarity below on (i) which transactions should be defined as a "derivative" for these purposes, (ii) what it means to be "in the business of trading" and "in the business of advising", in each case, in connection with OTC derivatives and (iii) what the minimum business conduct requirements should be for Professional Parties.

> *(i) Definition of "derivative":* As to which transactions should be defined as a "derivative" for these purposes, the Consultation Paper does not provide clarity, although a degree of insight is provided under section 6.1(a). CMIC is of the view that the definition of a "derivative" should, at a minimum, exclude all transactions which are not considered a derivative under the Model Scope and TR Rules Paper. In addition, as referred to and discussed in greater detail on pages 5-7 (inclusive) of the CMIC Model Scope and TR Rules Letter, there are additional transactions that should not be considered a "derivative".[16]
>
> *(ii) In the business of trading/advising OTC derivatives:* With respect to what it means to "be in the business of trading" an OTC derivative or "be in the business of advising" in connection with an OTC derivative, the proposal under sections 6.1 and 6.2 of the Consultation Paper is too broad. CMIC submits that (i) the definition of "trading in a derivative" should be limited to the entering into an OTC derivative transaction (including

[14] Based on published unaudited financial statements for the second quarter of fiscal 2013 for the 6 largest Canadian banks and derivatives market statistics for end-December 2012 published by The Bank for International Settlements. This figure is an approximation only and has not been adjusted to reflect double-counting or timing issues.

[15] See testimony of Christopher Giancarlo before the House Financial Services Subcommittee, noting that U.S. dealers are being shunned by foreign counterparties, who have both publicly and privately declared they will not register with U.S. regulators; available at http://financialservices.house.gov/uploadedfiles/hhrg-112-ba16-wstate-cgiancarlo-20121212.pdf. See also various media reports discussing the withdrawal of foreign counterparties from U.S. markets; available at http://online.wsj.com/article/SB10001424052970203400604578072221988442386.html and http://www.ft.com/intl/cms/s/0/a9a6f1be-ae2b-11e2-82b8-00144feabdc0.html#axzz2VFU6ZMqL.

[16] These include exchange traded derivatives, physical commodity transactions, "long dated" foreign exchange spot transactions, all gaming contracts and all insurance contracts. Please see our complete comments on the definition of a "derivative" in the CMIC Model Scope and TR Rules Letter.

novations of an existing OTC derivative transaction) as principal, and the business trigger should be limited to acting as a market maker or trading with the intention of being remunerated or compensated; and (ii) the definition of "advising" in connection with an OTC derivative transaction should be limited to providing customized, specific investment advice to an individual party in connection with the entering into of an OTC derivative transaction, and the business trigger should be limited to the frequent or regular provision of such advice where the provider of such advice is expected to be remunerated or compensated. It is CMIC's view that all the pension fund members of CMIC would not be considered "Professional Parties" and instead, are "end users" and should not be required to register in any circumstance.

(iii) Minimum business conduct requirements: The minimum business conduct requirements applicable to all Professional Parties would be those set out under section 7.2(b)(iii)(A) *(Know your Client/Counterparty)*, section 7.2(b)(iii)(C) *(Conflicts of Interest)*, section 7.1(c)(i) *(Compliance and Risk Management Systems)*, section 7.1(c)(iii) *(Recordkeeping)* and section 7.1(d) *(Honest Dealing)* of the Consultation Paper.

So long as Professional Parties deal with a qualified party,[17] no further requirements (which form the subject matter of the Consultation Paper)[18] would be imposed. Where Professional Parties deal with non-qualified parties, CMIC submits that suitability and fair dealing requirements (as set out under section 7.2(b)(iii)(B) and (D) of the Consultation Paper) should also be imposed. Additional requirements may also apply in such circumstances (though may not, in all cases, be necessary), such as registration, notice requirements to the relevant securities commission, the additional requirements set out under 7.2(b)(ii) of the Consultation Paper or proficiency requirements relating to a Professional Party or its traders/advisers dealing with non-qualified parties.

CMIC submits that the above approach is appropriate for the Canadian OTC derivatives market. As noted by the Committee in the Consultation Paper, derivatives are different than securities. The goal of a securities regulator is to provide protection to investors from unfair, improper or fraudulent practices and foster fair and efficient capital markets and confidence in capital markets".[19] The Canadian OTC derivatives marketplace has not demonstrated that there are any problems with regard to unfair, improper or fraudulent dealing, nor has there been a need to protect "investors" entering into derivatives transactions. The overwhelming majority of OTC derivatives transactions entered into in Canada are between qualified (sophisticated) parties. There is therefore not the same need to "protect" these "investors" as is the case in the securities market with retail investors.

As noted in our introductory remarks, registration of OTC derivatives counterparties is not listed as one of the G-20 commitments. The goals stated in the G-20 commitments relating to OTC derivatives in Pittsburgh[20] are to improve transparency in the derivatives market, mitigate systemic risk and protect against market abuse. CMIC submits that those goals would be effectively achieved through mandatory requirements for trade reporting, central clearing of standardized trades, minimum business conduct requirements and higher capital and margin requirements for certain non-centrally

[17] CMIC recognizes that different terminology is used in Canada in referring to the concept of a sophisticated party (such as "qualified party", "accredited investor", "accredited counterparty", and "permitted client"). Where the term "qualified party" is used throughout this letter, CMIC is referring to the concept of a sophisticated party generally, and is not advocating the use of one term or definition over another, other than as expressly set out in this letter.

[18] CMIC recognizes that there are different requirements for other areas of OTC derivatives reform, such as those relating to the G-20 commitments of trade reporting, central clearing and capital and collateral requirements.

[19] Statutory mandate of the Ontario Securities Commission. See http://www.osc.gov.on.ca/en/About_about_index.htm.

[20] See paragraph 13. http://www.g20.utoronto.ca/2009/2009communique0925.html.

cleared trades, and not by the imposition of registration requirements as set out in the Consultation Paper. In fact, we strongly believe that such registration requirements would have a negative impact on the liquidity of the Canadian market which could well produce the unintended consequence of increasing systemic risk.

Questions & Responses

Q1: Should investment funds be subject to the same registration triggers as other derivatives market participants? If not, what registration triggers should be applied to investment funds?

There are no investment fund[21] members of CMIC. Accordingly, CMIC has no comment on this and encourages other industry organizations to provide commentary to the Committee on this question.

Q2: What is the appropriate standard for determining whether a person is a qualified party? Should the standard be based on the financial resources or the proficiency of the client or counterparty? If the standard is based on financial resources should it be based on the net assets of the client or counterparty, gross annual revenues of the client or counterparty, or some other factor or factors?

CMIC feels strongly that the standards for determining whether a person is a qualified party should be as objective as possible and should not require any subjective assessments, such as a person's proficiency, experience or knowledge. If such subjective elements were included, it should not apply to all categories of the definition, but should only have limited application, and in every case, parties should be able to rely solely on representations made by a party with respect to such subjective matters. At a minimum, the definition of a "qualified party" under Canadian regulation (i) should capture all persons satisfying the requirements of an "Eligible Contract Participant" under Dodd-Frank, (ii) the definition of "qualified party" should be the same across all Provinces and (iii) include a definition of a "hedger" similar to the one found under the *Derivatives Act* (Quebec).[22]

Q3: Should registration as a derivatives dealer be subject to a *de minimis* exemption similar to the exemption adopted by U.S. regulators? Please indicate why such an exemption is appropriate.

If one of the goals of registration is to address financial stability and systemic risk, the registration process should not capture small derivatives dealers and therefore a *de minimis* exemption is appropriate. In Canada, market participants are limited in number as compared to the United States. Therefore, CMIC submits that it is not appropriate to impose requirements that unnecessarily deter participation in the market where such participant's business does not impact systemic risk.

In addition, if foreign market participants are ultimately required to register in Canada, CMIC is of the view that there should be a *de minimus* exemption. Foreign market participants provide much needed liquidity to the Canadian market, often offering the depth of products to larger market participants, such as pension funds, which Canadian sell-side counterparties are unable to offer. CMIC believes that if Canadian regulators ultimately require foreign market participants to register, liquidity in

[21] CMIC has pension fund members, however, these are large public sector pension funds which, in our view, are not the type of "investment funds" to which this question relates.

[22] Under s. 3(12) *Derivatives Act* (Quebec), a hedger is defined as "a person who, because of the person's activities, (a) is exposed to one or more risks attendant upon those activities, including supply, credit, exchange and environmental risks and the risk related to fluctuations in the price of an underlying interest; and (b) seeks to hedge that risk by engaging in a derivatives transaction, or a series of derivatives transactions, where the underlying interest is the underlying interest directly associated with that risk or a related underlying interest".

Canada would be significantly reduced, which would be harmful to Canadians. Again, a careful review of two years of trade reporting data before determining whether it is advisable to implement a registration regime would ensure a significant compression of liquidity is avoided.

Q4: Are derivatives dealer, derivatives adviser and LDP the correct registration categories? Should the Committee consider recommending other or additional categories?

CMIC is of the view that the LDP category is not appropriate for Canada. For example, some CMIC members that are public sector pension funds could potentially be considered to have substantial positions. However, it is clear that such buy-side end-users do not "make" derivatives markets. It is therefore unclear what risk is being addressed if such participants are required to register. CMIC does not believe that other or additional categories of registration are necessary.

Q5: Are the factors listed the correct factors that should be considered in determining whether a person is in the business of trading derivatives? Please explain your answer.

The factors listed are much broader than those required for a "swap dealer" under Dodd-Frank. The "directly or indirectly soliciting" category is not something that would indicate that a participant is dealing in derivatives. The Consultation Paper refers to advertising on the internet with the intention of encouraging trading as an example of an activity. This type of activity is associated with the retail securities market and is not something that is typically associated with "trading a derivative". CMIC submits that only where a party enters into a derivatives trade as principal should such activity qualify as "the business of trading derivatives". With regard to the factor "providing clearing services to third parties", please see our response to question 7 below.

Q6: The Committee is not proposing to include frequent derivatives trading activity as a factor that we will consider when determining whether a person triggers registration as a derivative dealer. Should frequent derivatives trading activity trigger an obligation to register where an entity is not otherwise subject to a requirement to register as a derivatives dealer or a LDP? Should entities that are carrying on frequent derivatives trading activity for speculative purposes be subject to a different registration trigger than entities trading primarily for the purpose of managing their business risks?

CMIC is of the view that factors should be based on the behaviour of a participant, rather than how often such participant trades. If frequency of trading was included as a factor and frequent hedgers (who are often end-users) are therefore made subject to registration when they otherwise would not be required to register, proper hedging could be discouraged. Such a result would be inconsistent with systemic risk mitigation. In CMIC's view, there is no necessary correlation between frequency of trading and the risks attached to that trading.

Q7: Is the proposal to impose derivatives dealer registration requirements on parties providing clearing services appropriate? Should an entity providing these clearing services only to qualified parties be exempt from regulation as a derivatives dealer?

CMIC submits that it is not necessary, and potentially harmful, to impose derivatives dealer registration requirements on parties providing clearing services. If clearing is mandated, access to central clearing counterparties will become critical. If dealer registration is required for parties providing clearing services, it may discourage entities, particularly foreign entities, from providing clearing services for Canadian market participants. Further, the CCP Paper proposes that central clearing counterparties are required to be recognized in Canada (where clearing for Canadian participants), and part of that recognition process includes a review of the risk management and membership criteria (among other things) of such central clearing counterparty by the Canadian securities regulator. In addition, other rules are being proposed relating to central clearing (in

particular, segregation and portability) which will also protect both clients and parties undertaking client clearing.

With regard to the second part of question 7, since CMIC is of the view that all parties dealing with qualified parties should be exempt from registration, our answer is yes.

Q8: Are the factors listed above the appropriate factors to consider in determining whether a person is in the business of advising on derivatives?

None of the CMIC members is in the business of solely providing derivatives advice. Accordingly, CMIC has no comment on this and encourages other industry organizations to provide commentary to the Committee.

Q9: Are the factors listed for determining whether an entity is a LDP appropriate? If not what factors should be considered? What factors should the Committee consider in determining whether an entity, as a result of its derivatives market exposures, could represent a serious adverse risk to the financial stability of Canada or a province or territory of Canada?

Since no equivalent category to the LDP category exists, to our knowledge, in any G-20 jurisdiction (other than the U.S.), we are very concerned about creating a unique registration regime feature in a smaller market like Canada. Therefore, as set out under question 4 above, it is CMIC's view that the LDP category is not appropriate for Canada.

Q10: Is the Committee's proposal to only register derivative dealer representatives where they are dealing with clients or when dealing with counterparties that are non-qualified parties appropriate?

As noted above in the section "General Comments", it is CMIC's view that registration requirements should be imposed only where a Professional Party deals with a non-qualified party. Even in such cases, the registration of individual representatives may not be necessary provided that the Professional Party has sufficient and appropriate compliance procedures in place to ensure that individuals dealing with such non-qualified party are proficient and have proper supervision.

Q11: Is it appropriate to impose category or class-specific proficiency requirements?

CMIC submits that the imposition of proficiency requirements, whether category or class specific requirements or general requirements for individuals, are of no benefit to OTC derivatives market participants and are unnecessary for the integrity of the OTC derivatives market as a whole. CMIC is unaware of any market conduct issues that such requirements are intended to address and no evidence has been presented to justify such requirements. To our knowledge, no other foreign jurisdiction, including under either Dodd-Frank or EMIR,[23] has imposed such detailed proficiency requirements with respect to OTC derivatives market participants. These are requirements that have worked well in, and are appropriate for, the securities market. However, CMIC submits that they are not appropriate or necessary for the Canadian OTC derivatives market where business models have relied upon internal risk management and governance rules to determine proficiency of individuals trading or advising in derivatives products. Further, as mentioned above, the overwhelming majority of OTC derivatives transactions in the Canadian market involve only sophisticated parties, who understand the fundamentals of derivatives markets and do not deal with anyone who does not

[23] European Market Infrastructure Regulation ("EMIR") adopted by the European Parliament on 29 March 2012, available at http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+TA+20120329+SIT-01+DOC+WORD+V0//EN&language=EN at Article 3.

demonstrate proficiency in the area. It may be the case that where a dealer is trading an OTC derivative with a non-qualified party, certain proficiency requirements might be warranted with respect to traders or advisers dealing directly with such non-qualified party.

Q12: Is the proposed approach to establishing proficiency requirements appropriate?

See our answer to question 11 above.

Q13: Is the Committee's proposal to impose a requirement on registrants to "act honestly and in good faith" appropriate?

CMIC is of the view that this requirement to act honestly and in good faith should apply to all market participants, whether they are registered or not.

Q14: Are the requirements described appropriate registration requirements for derivatives dealers, derivatives advisers and LDPs? Are there any additional regulatory requirements that should apply to all categories of registrants? Please explain your answers.

As mentioned above, CMIC strongly urges the CSA to defer the decision on whether to implement a registration regime until it has received and studied at least two years of trade repository information and determined whether there are market conduct issues which are not being addressed from a regulatory perspective. If it is ultimately determined that a registration regime is required, CMIC submits that such a requirement should be imposed only where a derivatives dealer trades (or a derivatives advisor advises in connection with) an OTC derivative transaction with a non-qualified party. In such limited circumstances, CMIC is of the view that the registration requirements are generally appropriate, except for the insurance requirement for the reasons set out below in our response to question 17. However, it would be more appropriate to impose requirements only where the CSA has determined that there are specific market conduct issues which are not being addressed under existing rules.

Q15: Should derivatives dealers dealing with qualified parties be subject to business conduct standards such as the ones described in part 7.2(b)(iii) above? If so, please explain what standards should apply.

Yes. See our commentary under "General Comments".

Q16: Do you have a preference between the two proposals relating to the regulation of a derivatives dealer trading with counterparties that are non-qualified parties? Is there another option to address the conflict of interest that the Committee should consider? Please explain your answer.

CMIC submits that the second alternative is the better approach as it is more transparent. The first alternative may be impossible to implement from a timing perspective when parties need to act quickly from a market perspective. In addition, this first alternative is dependent upon receiving advice from a registered adviser who would provide consultation services to a non-qualified party. It is CMIC's view that it would be difficult to find a registered adviser who would be available to provide such services, in particular as it is unlikely that such non-qualified party would be an existing client of the registered adviser.

With regard to the second alternative, it should be clarified that the derivatives dealer is not providing advice in informing the counterparty that it has the right to obtain independent advice before entering into a transaction. As well, it should be clarified that the non-qualified party can sign the acknowledgement up front as part of normal account opening procedures and protocols and

customary know your client processes, as opposed to a requirement to obtain an acknowledgement for every transaction.

Q17: Are the recommended requirements appropriate for registrants that are derivatives dealers? If not please explain. Are there any additional regulatory requirements that should apply to registered derivatives dealers?

See our answer to question 11 for CMIC's views on proficiency requirements. CMIC submits that the insurance requirements under section 7.1(b)(iii) of the Consultation Paper are not appropriate for the OTC derivatives market where the vast majority of collateral held by a dealer would be held in electronic form. The following additional regulatory requirements should apply to registered derivatives dealers: (i) exposure valuations that are consistent with the ISDA definition of "Exposure" should be made available to any non-qualified counterparty on demand, and (ii) timely confirmations of transactions should be provided to counterparties.

Q18: Are the recommended requirements appropriate for registrants that are derivatives advisers? If not please explain. Are there any additional regulatory requirements that should apply to registered derivatives advisers?

None of the CMIC members is in the business of solely providing derivatives advice. Accordingly, CMIC has no comment on this and encourages other industry organizations to provide commentary to the Committee.

Q19: The Committee is recommending that foreign resident derivative dealers dealing with Canadian entities that are qualified parties be required to register but be exempt from a number of registration requirements. Is this recommendation appropriate? Please explain.

Imposing additional registration requirements for foreign resident participants will severely restrict liquidity in the Canadian market. As mentioned in the "General Comments" section above, a significant portion of liquidity in the Canadian market is provided by non-domestic participants.[24] If foreign resident derivatives dealers dealing with qualified parties are required to register, even though they may be exempt from a number of registration requirements, there is a serious risk that they will choose not to deal with Canadian market participants. This will have the effect of reducing liquidity in the Canadian market, making it more difficult for end users to enter into hedges. Further, foreign resident derivative dealers will be regulated by their home jurisdiction and imposing further registration requirements under the Canadian regime for such dealers could be inconsistent with comity and compromise the ability of Canadian market participants to obtain substitute compliance in foreign jurisdictions.

Q20: Is the Committee's recommendation to exempt foreign resident derivatives dealers from Canadian registration requirements where equivalent requirements apply in their home jurisdictions appropriate? Please explain.

It is CMIC's view that the appropriate test here is not that the foreign resident derivatives dealers have "equivalent" requirements in their home jurisdiction, but "comparable" or "similar" requirements. The concept of substitute compliance and reciprocity amongst regulators in respect of G-20 commitments will be made difficult if jurisdictions (especially relatively smaller jurisdictions, such as Canada) require

[24] For example, as of February 1, 2011, almost half of all Canadian dollar denominated interest rate swaps are not entered into by any of the big six Canadian banks. Source: CMIC "Data Analysis Report", February 1, 2011; Bank for International Settlements Triennial Survey June 2010.

that the foreign jurisdiction have "equivalent" requirements. Requirements that achieve comparable results should be sufficient.

Q21: Should foreign derivatives dealers or advisers not registered in Canada be exempt from registration requirements where such requirements solely result from such entities trading with the Canadian federal government, provincial governments or with the Bank of Canada?

Exemption from registration solely on the basis of a derivatives dealer trading with the Canadian federal government, provincial governments or with the Bank of Canada is not appropriate. This bifurcates market liquidity for sovereign entities versus other end-users. However, as stated in the "General Comments", CMIC is of the view that a Professional Party should be exempt from registration if it deals with any qualified party (and not just a Canadian sovereign entity or the Bank of Canada).

Q22: Is the proposal to exempt crown corporations whose obligations are fully guaranteed by the applicable government from registration as an LDP and, in the circumstances described, as a derivatives dealer appropriate? Should entities such as crown corporations whose obligations are not fully guaranteed, foreign governments or corporation owned or controlled by foreign governments benefit from comparable exemptions? Please provide an explanation for your answer.

As stated above in our response to question 4, CMIC is of the view that there should not be a separate LDP category of registration. Further, as indicated in our response above to question 21, CMIC is of the view that creating special exemptions for specific entity types bifurcates liquidity in the market. Exemptions should be based upon whether a party is a qualified party, which in turn should be determined by objective criteria.

Q23: Are the proposed registration exemptions appropriate? Are there additional exemptions from the obligation to register or from registration requirements that should be considered but that have not been listed?

See responses to questions 21 and 22 above, as well as our submissions in the "General Comments" section of this letter.

CONCLUSION

CMIC believes that continued engagement with the CSA is fundamental to the development of a regulatory framework that meets the G-20 commitments and achieves the intended public policy purposes. Thoughtful inclusion by regulators of the themes set out in the Overview section of this letter will meaningfully contribute to the success of the development of an effective Canadian framework for the regulation of key participants in the OTC derivatives market.

As we have noted in our prior submissions, each subject relating to OTC derivatives regulation is interrelated with all other aspects. As such, CMIC reserves the right to make supplementary submissions relating to the proposed registration regime following publication of further consultation papers and model and draft rules.

CMIC hopes that its comments are useful in the development of the regime for the regulation of the OTC derivatives market and that the CSA takes into account the practical implications for all market participants who will be subject to such regulation. CMIC welcomes the opportunity to discuss this response with representatives from the CSA.

The views expressed in this letter are the views of the following members of CMIC:

Bank of America Merrill Lynch
Bank of Montreal
Caisse de dépôt et placement du Québec
Canada Pension Plan Investment Board
Canadian Imperial Bank of Commerce
Deutsche Bank A.G., Canada Branch
Healthcare of Ontario Pension Plan
HSBC Bank Canada
JPMorgan Chase Bank, N.A., Toronto Branch
Manulife Financial Corporation
National Bank of Canada
OMERS Administration Corporation
Ontario Teachers' Pension Plan Board
Royal Bank of Canada
The Bank of Nova Scotia
The Toronto-Dominion Bank