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Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumers Affairs Authority of Saskatchewan
Manitoba Securities Commission
New Brunswick Securities Commission
Nova Scotia Securities Commission
Ontario Securities Commission

Dear Sirs/Mesdames:

Comments on Model and Proposed Rules Concerning Derivatives Data Reporting

This letter is in response to the request for comments regarding Multilateral CSA Staff Notice 91-302 – *Updated Model Rules – Derivatives Product Determination and Trade Repositories and Derivatives Data Reporting* published on behalf of the Alberta Securities Commission, the British Columbia Securities Commission, the New Brunswick Securities Commission, the Nova Scotia Securities Commission and the Financial and Consumer Affairs Authority of Saskatchewan as well as the province-specific proposed rules concerning derivatives data reporting published by the Autorité des marchés financiers of Quebec[1], the Manitoba Securities Commission[2] and the Ontario Securities Commission[3] (collectively referred to herein as the "TR Rule").

As counsel to counterparties ranging from global financial institutions and pension plans to commodity producers and investment funds, Osler, Hoskin & Harcourt LLP has had extensive involvement with derivatives transactions, albeit from a legal perspective. In this letter, we comment from a regulatory standpoint on certain aspects of the proposed TR Rule. Our comments address the following:

- harmonization within Canada;
- process for obtaining exemptive relief;
- definition of Local Counterparty;

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[1] Draft AMF Regulation 91-507 respecting Trade Repositories and Derivatives Data Reporting.

[2] Proposed MSC Rule 91-507 *Trade Repositories and Derivatives Data Reporting*.

[3] Proposed OSC Rule 91-507 *Trade Repositories and Derivatives Data Reporting*.

- reporting by Local Counterparties;
- data availability;
- public dissemination of block trade data;
- reporting derivatives transactions with securities underliers; and
- data to be reported.

I. Need for Harmonization within Canada

It remains unclear the extent to which "minor variances" to the TR Rule will be made by securities regulatory authorities in finalizing and adopting their own local rules. Variances introduced at the adaptation and implementation stages may result in non-trivial distinctions in the regimes ultimately adopted by the jurisdictions. While we appreciate that local environments differ, we respectfully submit that the national (and, indeed, global) scope of the derivatives market argues for regulation that is harmonized to the greatest extent possible across the country.

There is also a lack of guidance on whether the final rules to be adopted by each province will be brought into force simultaneously. Given the inter-provincial nature of many derivative transactions, implementation that does not occur simultaneously may lead to uncertainty regarding which rules apply to a given transaction or counterparty, as well as the potential for regulatory arbitrage.

Finally, we note that CSA responses to comments received on CSA Staff Consultation Paper 91-301 Model Provincial Rules – *Derivatives Product Determination and Trade Repositories and Derivatives Data Reporting* (the "Draft Model Rules") suggest that the establishment of a "passport"-type system for facilitating inter-provincial recognition of orders and exemptions is outside the scope of the TR Rule. We would respectfully submit that such a system is necessary, particularly in light of the CSA's current position that certain matters be considered on a case-by-case basis under the exemption power in section 41 of the TR Rule (discussed in greater detail in item II below).

II. Process for Exemptive Relief

In the CSA responses to comments received on the Draft Model Rules, there were several references to matters that would be considered on a case-by-case basis under the exemption power in section 41 of the TR Rule. These include:

- "substituted compliance" when reporting derivatives data, including reporting data concerning pre-existing trades, reported pursuant to foreign rules;

- reporting information that may not be disclosed due to foreign data and confidentiality laws; and

- public dissemination of block trade data.

It must be emphasized that derivatives transactions increasingly occur in a high-paced, electronic trading environment. It is uncommon for a particular derivatives transaction to have a lead time of weeks or months. Moreover, once a transaction occurs, section 28 of the TR Rule requires real-time reporting. Given this reality, we are concerned that there will be insufficient time for a local counterparty to obtain exemptive relief from the TR Rule in order to, for example, (i) comply with data protection and confidentiality laws of a foreign jurisdiction or (ii) prevent the disclosure of block trade data that, if disclosed, would frustrate a party's ability to properly hedge its position. In addition to these timing concerns, we are also concerned that the process for obtaining discretionary exemptive relief under section 41 of the TR Rule would be expensive and the results would vary by province and territory.

We therefore respectfully submit that the CSA should develop a process for local counterparties to seek exemptive relief in a timely and efficient manner, with such exemptive relief 'passported' into other CSA jurisdictions. In the alternative, the CSA should amend the TR Rule to specifically address issues of substituted compliance, confidentiality laws, and public dissemination of block trade data.

III. Definition of "Local Counterparty"

We appreciate the many changes made to the definition of "local counterparty" in the TR Rule in response to comments received on the Draft Model Rules. However, we are concerned that the revised definition remains somewhat vague and overly broad.

In part (a) of the definition, it is not clear as to why a person or company should be considered a "local counterparty" simply by virtue of being organized under the laws of the local province. There are many examples of limited partnerships, trusts and corporate entities that are organized under provincial law, but have a head office or principal place of business outside that province, or that have all or substantially all of their trustees, partners, shareholders, directors and/or officers located outside that province. Inclusion of the reference to being organized under the laws of a particular province also does not take into account federal entities, such as corporations incorporated under the *Canada Business Corporations Act.* We therefore respectfully submit that part (a) of the definition should instead refer to "a person or company, other than an individual, that has its head office or principal place of business in [Province X]".

With respect to part (b) of the definition, we respectfully suggest that the following wording is unclear and potentially misleading:

> "[a counterparty] subject to regulations providing that a person or company trading in derivatives must be registered in a category of registration prescribed by the regulations".

First, it is not clear to which regulations this wording refers. Second, in certain provinces, such as Ontario, the requirement to register is found in the provincial securities act, not regulations promulgated under that act. On the assumption that part (b) is designed to capture entities registered as derivatives dealers and perhaps large derivatives participants, we would suggest the following alternative wording:

> "the counterparty is registered under [Province X] securities legislation as a dealer, large derivatives participant or an equivalent category of registration prescribed by [Province X] securities legislation".

IV. Reporting by Local Counterparties

Section 35 of the TR Rule requires all local counterparties to a reportable transaction to report valuation data. While we acknowledge that reporting can be delegated to a third party under subsection 27(4) of the TR Rule, we nevertheless expect it to be burdensome for certain local counterparties to comply with the valuation data reporting requirement. We therefore respectfully request that the CSA consider whether the potential benefit in receiving (potentially) two valuation points for a particular transaction outweighs the significant cost and challenge for local counterparties, particularly small end users, to report valuation data. We respectfully suggest that the TR Rule should be implemented in such a way that valuation data is initially reported only by the reporting counterparty. If, after a period of time, the CSA concludes that more data is necessary, it could require valuation data reporting by all local counterparties.

Related to the point above, we question whether it is necessary for local counterparties that are affiliated entities to report valuation data. Local counterparties may not have, and may not need, processes for calculating and reporting valuation data for transactions with affiliated entities. We would therefore respectfully suggest that, in transactions between affiliated entities, only one local counterparty need report valuation data. Also, we would respectfully request that the CSA consider modifying the timing requirements for reporting both life-cycle data and valuation data for transactions between affiliated entities. We would suggest that data from such transactions need be reported on a quarterly, not daily, basis.

Finally, subsection 35(1) requires a local counterparty (including a local counterparty that is not a dealer) to report valuation data on a daily basis if the transaction is cleared. However, subsection (2) permits a local counterparty that is not a dealer to report valuation data on a quarterly basis if the transaction is not cleared. In our view, this discrepancy will create a significant disincentive for local counterparties that are not dealers to engage in cleared transactions. Therefore, section 35(1) should be modified to

permit a local counterparty that is not a dealer to report valuation data for a cleared transaction on a quarterly, not daily, basis.

V. Data Availability

Subsection 37(3) of the TR Rule requires that a local counterparty must take any action necessary to ensure that the securities regulatory authority has access to all derivatives data reported to a designated trade repository for transactions involving the local counterparty. It is unclear why such a provision is necessary. All data reported to a designated trade repository will already be available to the securities regulatory authority under subsection 37(1) and it is uncertain what action a local counterparty could take to make that data available. Therefore, we respectfully submit that subsection 37(3) should be struck from the TR Rule.

VI. Public Dissemination of Block Trade Data

As drafted, section 39 of the TR Rule does not provide any exceptions for block trade data. In the CSA responses to comments received on the Draft Model Rules, CSA Staff rejected an exception for block trade data on the basis that case-by-case exemptions under section 41 would be satisfactory. We respectfully submit that section 39 should be amended to provide certain exceptions to public reporting for block trades.

As recognized by CSA Staff, the purpose of publication delays in section 39 is to provide counterparties with sufficient time to enter into any offsetting transaction that may be necessary to hedge their positions. However, large transactions may require additional time to hedge, and reporting the full notional value of such transactions could have distortive effects on the market. In the United States, the Securities and Exchange Commission ("SEC") and Commodity Futures Trading Commission ("CFTC") are currently phasing in public reporting requirements that contemplate certain exceptions for block trades of sufficient size. We are therefore concerned that, to the extent that U.S. regulators do not require certain public disclosures, to do so in Canada, even with a delay, would lead to inadvertent signalling to the international derivatives market.

We respectfully suggest that the CSA should amend the TR Rule to provide that notional caps be applied to public reporting of large transactions. Together with a mechanism for delaying reporting, the advantage of this approach is that it will provide transparency as well as preserve the ability of large investors and companies to hedge their risks in a cost-effective way.

We acknowledge that transaction data is necessary to determine the appropriate level of any notional caps. We therefore respectfully suggest that public reporting of transaction data under section 39 be delayed for a period of one year from the implementation date of the TR Rule, during which time the CSA can analyze transaction data and determine

appropriate caps and thresholds, as well as identify any other amendments to the TR Rule that may be necessary.

VII. Reporting Derivatives Transactions with Securities Underliers

We recognize that the model and proposed rules for derivatives product determination do not distinguish between securities-based derivatives and other underlying asset classes of derivatives. Nevertheless, we respectfully request that amendments be made to the TR Rule to delay the implementation date for transaction reporting on securities-based derivatives (e.g., security-based swaps based on a single-name or narrow-based index). We make this request on the basis that these types of transactions are not yet reported in the United States. While Canadian securities regulators are not beholden to their U.S. counterparts, it must be reiterated that there will be significant technology, legal, compliance and related business costs for parties to comply with the TR Rule. Due to the global nature of derivatives trading, these costs will be aggravated by an inconsistent approach to regulation between Canadian and non-Canadian securities regulators. A delayed, or phased-in, approach to transaction reporting in Canada that is synchronized with United States reporting requirements would facilitate efficient global markets and defray some of the costs that local counterparties will otherwise face.

VIII. Data to be Reported

Further to items II and VII above, we respectfully request that the CSA work with the CFTC and SEC to adopt a system of "substituted compliance", which would apply where a transaction reportable under the TR Rule is also reported to a designated trade repository pursuant to CFTC or SEC rules. Under this system of substituted compliance, there would be no need for separate reports to a designated trade repository for Canadian purposes, since Canadian securities regulators would have access to CFTC and SEC transaction data.

The alternative to a substituted compliance regime would be to provide for the data fields required pursuant to the TR Rule to be identical to the data fields required pursuant to equivalent CFTC and SEC rules. With due respect to Canadian and U.S. securities regulators, we see no reason for there to be any substantive differences between the data fields required under the TR Rule and under CFTC and SEC rules. If there are any reasons for there to be differences in data fields, such reasons must be weighed against the significant costs that reporting counterparties will incur to create similar, but not identical, reporting applications and processes for the two countries.

Given the already considerable costs for derivatives counterparties to comply with the TR Rule, we respectfully request that the CSA adopt the system of substituted compliance described above, or, in the alternative, modify data fields required pursuant to the TR Rule to be identical to data fields required pursuant to equivalent CFTC and SEC rules.

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Thank you for the opportunity to comment on the TR Rule. If you have any questions or comments, please contact Mark DesLauriers (416-862-6709 or mdeslauriers@osler.com) or Blair Wiley (416-862-5989 or bwiley@osler.com).

Yours very truly,

Osler, Hoskin &Harcourt LLP