April 19, 2016

Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumer Services Commission (New Brunswick)
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Nova Scotia Securities Commission
Nunavut Securities Office
Ontario Securities Commission
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

Me Anne-Marie Beaudoin
Corporate Secretary
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Josée Turcotte
Secretary
Ontario Securities Commission
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E-mail: comments@osc.gov.on.ca

Dear Sirs/Mesdames:

Re: Canadian Securities Administrators ("CSA") Staff Notice and Request for Comment – Proposed National Instrument 94-102: *Derivatives: Customer Clearing and Protection of Customer Collateral and Positions* and related Proposed Companion Policy 94-102CP (collectively, the "Proposed Instrument")

Substitute Compliance

The Canadian Market Infrastructure Committee ("**CMIC**")[1] welcomes the opportunity to comment on the Proposed Instrument[2]. Given that the OTC derivative clearing infrastructure and clearing

[1] CMIC was established in 2010, in response to a request from Canadian public authorities, to represent the consolidated views of certain Canadian market participants on proposed regulatory changes in relation to over-the-counter ("**OTC**") derivatives. The members of CMIC who are responsible for this letter are: Alberta Investment Management Corporation, Bank of America Merrill Lynch, Bank of Montreal, Bank of Tokyo-Mitsubishi UFJ (Canada), Caisse de dépôt et placement du Québec, Canada Pension Plan Investment Board, Canadian Imperial Bank of Commerce, Citigroup Global Markets Inc., Deutsche Bank A.G., Canada Branch, Fédération des Caisses Desjardins du Québec, 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, Public Sector Pension Investment Board, Royal Bank of Canada, Sun Life Financial, 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 over-the-counter ("**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, including both domestic and foreign owned banks operating in Canada. As it has in all of its submissions, this letter reflects the consensus of views within CMIC's membership about the proper Canadian regulatory regime for the OTC derivatives market.

intermediaries are largely concentrated outside of Canada, CMIC wishes to reiterate, in the context of this Proposed Instrument, its position concerning the importance of an effective substitute compliance regime. To the extent foreign clearing intermediaries and foreign clearing agencies that clear transactions on behalf of local customers are faced with customer collateral requirements in Canada that are stricter than, conflict with, or duplicate the customer collateral requirements in their home jurisdiction, such intermediaries and clearing agencies may decide that Canadian rules are overly burdensome. This could lead to such intermediaries and clearing agencies deciding not to deal with Canadian customers, or charge higher fees, which would negatively affect access to clearing at a reasonable cost for Canadian market participants.

To that end, CMIC supports (i) the narrowing of the scope of the Proposed Instrument from the previous version of the rule such that Canadian clearing intermediaries are not subject to the rule if they are not clearing a transaction with a local customer, and (ii) the inclusion of new substitute compliance provisions. With regard to substitute compliance, CMIC would support the CSA identifying in Appendix A the laws of the major OTC derivatives jurisdictions, such as the United States and Europe. In addition, CMIC would also support the CSA, in determining which provisions of the Proposed Instrument will benefit from substitute compliance, taking a holistic approach and concluding that foreign customer protection rules qualify for substitute compliance as long as they offer the same level of overall protection as set out under the Proposed Instrument. If, for example, the rules of a foreign jurisdiction do not require that the books and records of a clearing intermediary record all of the items set out in Section 13(3) of the Proposed Instrument, CMIC submits that such fact alone should not disqualify the foreign rules from substitute compliance of Section 13 of the Proposed Instrument.

Customer Collateral Report - Regulatory

Section 25 of the Proposed Instrument provides that direct and indirect intermediaries receiving customer collateral must electronically file, on a monthly basis, a completed Form 94-102F1 and Form 94-102F2, respectively. These forms require direct and indirect intermediaries to report customer collateral on an individual customer basis. However, we note that futures commission merchants ("**FCMs**") under Dodd Frank are required to report customer positions to the U.S. Commodity Futures Trading Commission (the "**CFTC**") and to their designated self-regulatory organization only on an aggregate basis and not on an individual customer basis.[3] In light of this, CMIC recommends that Forms 94-102F1 and 94-102F2 be modified such that only the aggregate total of customer collateral positions will have to be reported by direct and indirect intermediaries.

At the very least, if the above recommendation is not accepted, CMIC believes that section 25 of the Proposed Instrument should be one of the sections listed in Appendix A of the Proposed Instrument for which substitute compliance is available for clearing intermediaries that are in compliance with the requirements of Dodd Frank.

Perfection of Cash Collateral

Finally, it would be remiss if we were to submit a comment letter on the issue of customer collateral without taking the opportunity to comment on the importance of amending the personal property security legislation in Canada to permit the perfection by way of control of a security interest in cash

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[2] See Notice and Request for Comment available at: http://www.osc.gov.on.ca/en/SecuritiesLaw_csa_20160121_94-102_derivatives-customer-collateral.htm.

[3] See CFTC Regulation 22.2(g) and corresponding Statement of Cleared Swaps Customer Segregation Requirements and Funds in Cleared Swaps Customer Accounts under 4d(f) of the U.S. Commodity Exchange Act contained in the Form 1-FR-FCM .

collateral held outside a securities account.[4] As we noted in our prior response letter[5], it has become market standard for parties to rely on the absolute transfer and right of set-off mechanic in order to have priority with respect to cash collateral. When using that mechanic, in order to avoid recharacterization, it is recommended that the "secured party" treat the cash as property of the "secured party" and not as property of the "pledgor". Best practices dictate that the account in which such cash is held should not be in the name of the "pledgor" or refer to the cash as belonging to the "pledgor". CMIC acknowledges that the Proposed Instrument includes a wording change to try and address this issue by providing that the clearing agency must "treat any property transferred as collateral by or on behalf of the customer", instead of the previous requirement that all customer collateral be held in a "segregated account clearly identifying the name of each customer or otherwise indicating that the property in the account is customer collateral". However, CMIC is still concerned about the potential risk that such arrangements could be recharacterized as creating a security interest which could lead to secured parties losing their priority with respect to cash collateral.

We acknowledge that amending personal property security legislation is outside the jurisdiction of the CSA. However, we encourage the CSA to impress upon the provincial governments how important such amendments are to the clearing process, the protection of customer collateral and ultimately, satisfying Canada's G20 commitments in an effective manner.

CMIC welcomes the opportunity to discuss this response with you. The views expressed in this letter are the views of the following members of CMIC:

Alberta Investment Management Corporation
Bank of America Merrill Lynch
Bank of Montreal
Bank of Tokyo-Mitsubishi UFJ (Canada)
Caisse de dépôt et placement du Québec
Canada Pension Plan Investment Board
Canadian Imperial Bank of Commerce
Citigroup Global Markets Inc.
Deutsche Bank A.G., Canada Branch
Fédération des Caisses Desjardins du Québec
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
Public Sector Pension Investment Board
Royal Bank of Canada
Sun Life Financial
The Bank of Nova Scotia
The Toronto-Dominion Bank

[4] This issue applies in Canada to all provinces and territories, other than the Province of Quebec. On April 21, 2015, legislation was adopted in the Province of Quebec whch came into force on January 1, 2016 allowing a secured party to perfect by way of control a security interest in bank deposits and cash transferred to secure an obligation.

[5] CMIC letter dated March 19, 2014 to CSA Staff Notice 91-304 Model Provincial Rule – Derivatives: Customer Clearing and Protection of Customer Collateral and Positions; Available at: http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20140319_91-304_canadian-market-infrastructure.pdf