CCUA ACCF
Canadian Credit Union Association
Association canadienne des coopératives financières

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August 31, 2017

Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Manitoba Securities Commission
New Brunswick Securities Commission
Newfoundland and Labrador Superintendent of Securities, Northwest Territories
Nova Scotia Securities Commission Superintendent of Securities
Ontario Securities Commission
Registrar of Securities, Prince Edward Island
Financial and Consumer Affairs Authority, Saskatchewan
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Nunavut

Me Anne-Marie Beaudoin
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Grace Knakowski
Secretary
Ontario Securities Commission
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comments@osc.gov.on.ca

Dear Sirs and Mesdames:

RE: Canadian Securities Administrators Proposed National Instrument 93-101

On April 4, 2017, the Canadian Securities Administrators ("the Securities Administrators") issued for comment proposed national instrument 93-101 Derivatives: Business Conduct and its associated companion policy 93-101CP (NI 93-101 and NI 93-101CP). The Canadian Credit Union Association (CCUA) welcomes this opportunity to provide the Securities Administrators with comments on the proposed national instrument.

The Canadian Credit Union Association is the national trade association for 278 co-operatively structured (i.e., one-member, one vote) credit unions in Canada outside of Quebec. Together, these

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credit unions control more than $205 billion in assets and collectively serve more than 5.6 million member/owners.

With one notable exception, credit unions are provincially-chartered co-operative not-for-profit financial institutions that exist to serve their members.[1] While credit unions generate profits for prudential and growth reasons, their primary objective is to meet the needs of their members. For 13 years running, credit unions have earned the top spot in the Ipsos "Best Banking" Awards[2] and have similarly been rated the top service provider in repeated surveys of Canadian Federation of Independent Business (CFIB) members.[3]

Credit unions in turn own and control provincial or regional centrals that provide them with wholesale financial services, liquidity management, payments processing and trade association services. These central entities include Atlantic Central (for credit unions in the Atlantic provinces), Central 1 Credit Union (for credit unions in Ontario and British Columbia) and Centrals in each of Manitoba, Saskatchewan and Alberta. Credit unions also own a federally-regulated bank called Concentra that provides wholesale financial and trust solutions to credit unions across Canada. This submission has been prepared in consultation with credit unions, Centrals and Concentra.

General Comments on the Proposed Instrument

With respect to the questions posed in CSA Notice and request for comments, we direct most of our attention to the question of the applicability of the proposed instrument and the possibility of an exemption under section 45 in Part 7 of NI-93-101. For the reasons described below, we think there are reasonable grounds for exempting the very few credit unions that could be construed as "dealers" or "advisors" from this instrument. Alternatively, we recommend *de minimus* exemption thresholds.

Notwithstanding these arguments, we offer some general comments on other elements of the proposed instrument. We are, for example, generally supportive of the two-tiered approach (Questions 1, 3 and 4) recognizing the different needs and expectations of more sophisticated end-users. We also are supportive of the ability of individuals to represent, in writing, their knowledge

[1] In 2016, the Caisses Populaires Acadiennes became a federal credit union under the trade name of UNI Financial Cooperation.
[2] See https://ccua.com/media/2017_08_29_ipsos_best_banking_awards.
[3] For the most recent CFIB survey results, see http://www.cfib-fcei.ca/english/article/8817-battle-of-the-banks-credit-unions-among-the-best-for-small-business.html. For a news story on this topic, see: http://business.financialpost.com/management/credit-unions-lead-the-pack-in-servicing-entrepreneurs-cfib-survey/wcm/b5f0256c-af66-4c1d-a4c2-f02bb34b7cb1.

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and experience in evaluating the "characteristics of the derivatives to be transacted." That is, our experience shows that there is a class of individuals who are capable of making informed, suitable decisions around the two products we discuss below (foreign exchange transactions and interest rate swaps).

Aligned with our arguments for a *de minimus* exemption, we are concerned about the reporting burden of providing daily valuations to the derivative party and the proposed information (question 9) on the inputs and assumptions that were used to create the valuations. As we discuss below, the credit unions that offer these products to their members do so largely based on a demand for these services by the member/customer. In the case of agricultural producers, for example, they purchase currency derivatives with the expectation of taking delivery of the currency, not to speculate in the asset. Requiring credit unions to provide them with daily valuations and the underlying inputs/assumptions would be unnecessarily burdensome. At a minimum, we would urge CSA members to consider arrangements that would allow central entities or Concentra – which again, generally make available the platforms where derivatives are transacted at the credit union level – to compile this information and make it available on behalf of credit unions.

Credit Union Applicability/Exemption

The vast majority of CCUA's 278 credit union members use derivative products strictly for their own hedging purposes. In the language of the multilateral instrument 96-101 ("*Trade Repositories and Derivatives Data Reporting*" or MI 96-101) requirements, credit unions are the local counterparty and the Centrals are the reporting counterparty for these derivative transactions.

The majority of credit unions are – from the perspective of NI 93-101 – the "derivative parties" that obtain services from a derivatives "dealer" or "advisor". They are the intended beneficiaries of the proposed market conduct rules and qualify for the "end user" exemption outlined in section 39: they do not solicit or otherwise transact in derivatives on behalf of another person or entity nor do they advise on these products, make available regular price quotes, facilitate/intermediate transactions with another person or company, or facilitate clearing of a transaction in a derivative through a clear agency for some other entity.

That said, *some* credit unions do offer *some* products to members that could be subject to the compliance expectations outlined in NI 93-101. Before turning to these products, it is important to stress again that the vast majority of credit unions focus on providing their members with products

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that fall clearly outside the definition of "derivative"[4] including, notably deposit-based and loan-based products.

In discussions with the members of our trade association, participants identified three types of products that might be construed as (a) meeting the definition of "derivative" and (b) be delivered by credit unions in such a way that they fall under the scope of the proposed market conduct rules. These are: currency derivatives, interest rate swaps on loan products, and index-linked term deposit accounts. In all three instances, the products are typically made available with the assistance of a central or Concentra either through a white-label platform (currency derivatives) or other means.

After careful investigation, we concluded that index-linked products do *not* meet the definition of derivative because they are fully-insured (by provincial deposit insurers) deposit products. Under CSA Multilateral Instrument 91-101, *Derivatives: Product Determination* (MI 91-101), deposit products are prescribed as not being derivatives by subparagraph 2(f).[5] Moreover, the delivery of these products do not satisfy most of the criteria used to determine whether an entity is a "derivative advisor" or "derivative dealer."

In the table below, we evaluate the credit union's role in delivering these products relative to the "derivative advisor/dealer" criteria. These criteria are referred to as a "non-exhausting list of factors" that should be "applied holistically" in the companion document. On our conversations with members, we attempted to obtain estimates of the number credit unions offering one or more of these two aforementioned products. Based on this effort, we estimated a total of 11 credit unions currently offer currency derivatives to their members. This is less than 4% of 280 CCUA's credit

4 In CSA Multilateral Instrument 91-101, Derivatives: Product Determination, a contract or instrument that is "evidence of a deposit" is considered an "excluded derivative." Similarly, "additional contracts not considered to be derivatives" includes – according to the companion policy – "a consumer or commercial contract to...obtain a loan or mortgage, including a loan or mortgage with a variable rate of interest, interest rate cap, interest rate lock or embedded interest rate option."

5 Paragraph 2(f) reads: A contract or instrument is prescribed not to be a derivative if it is "evidence of a deposit issued by a credit union or league to which the Credit Unions and Caisses Populaires Act, 1994 or a similar statute of Canada or a jurisdiction of Canada (other than Ontario) applies..." In Saskatchewan, however, a view emerged in the context of MI 96-101 that ILA deposits were not "specified derivatives" for the central but were for credit unions. This perspective appears to be grounded in the fact that SaskCentral is exempt from the Securities Act, 1998 leaving only credit unions as possible reporting entities. Notwithstanding this perspective, we think that for the purposes of MI 93-101, this matter should be revisited since it is a market conduct rule and not a reporting rule and ILA are clearly deposit products insured by provincial deposit insurers. There is no exposure risk to the member/owner/client. Further, we understand that there are discussions underway to provide credit unions with an exemption from the application of MI 96-101 based on arguments similar to those presented here: the ILAs represent small dollar activity amounts that do not justify the related regulatory burden and, in any case, the underlying data are already effectively captured in reporting to the trade repository.

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union members. In addition, we understand that usage at these 11 credit unions is limited. For example, of the three credit unions that offer currency derivatives in Manitoba and Saskatchewan, only one credit union has more than three members that utilize the product. While we do not have estimates on the number of credit unions that offer interest rate swaps to their members, there is good reason to believe that fewer than 11 of them do and, moreover, there probably is considerable overlap with the credit unions that offer currency derivatives.

Requirement to be a derivatives dealer/advisor	**Currency hedging**	**Interest rate swaps**
	Provide FX forwards to members	Hedge risks associated with treasury activities
Made available to members/customers?	Yes, typically agricultural or business members.	Yes, typically larger commercial members.
Routinely provides price quotes?	Not directly. Centrals/Concentra make available platform.	Not directly. Credit unions works through a Central/Concentra intermediary.
Acting as a market maker?	No, back-to-backing transaction with national banks, who are the market makers.	No, back-to-backing transaction with national banks, who are the market makers.
Engaging in an organized and repetitive manner?	No, Transactions are infrequent, *ad hoc* and for commercial purposes, not speculation.	No, Transactions are infrequent, *ad hoc* and for commercial purposes, not speculation.
Facilitating or intermediating transactions?	Yes, credit union facilitates member access to service through platform but is mostly demand-led process.	Yes, credit union facilitates access to swap but demand-led process.
Transacting with the intention of being compensated?	Yes. Credit unions may receive a fee from platform provider for transaction.	Yes. Credit unions may receive a fee from platform provider for transaction.
Directly or indirectly soliciting in relation to derivatives transactions?	Yes. Largely a member initiated process (i.e., demand-led)	Yes. Largely a member-initiated process (i.e., demand-led)

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Engaging in activities similar to a derivatives adviser or derivatives dealer?	Yes.	Yes
Providing derivatives clearing services?	No	No

In weighing these criteria, we are mindful of the CSA's comment that not all the factors "necessarily carry the same weight or that any one factor will be determinative." That is, we take a holistic approach to weighing the criteria. We are also cognizant of the extent to which the credit union engage "in the activities discussed above in an organized and repetitive manner."

Based on the table analysis, we think there are reasonable grounds for arguing that those credit unions that make these products available should not be defined as derivative "dealers" or "advisors" and should, therefore, fall outside the scope of the proposed instrument. As noted in the table, credit unions make available these products largely "on demand" to provide the full suite of services demanded by their commercial and agricultural members as well as more wealthy individuals. If they did not offer these services, they would risk losing those members to competitors. It is also worth bearing in mind that they do not themselves operate the platforms (where applicable), are not themselves the market maker nor the entity offering the quotes (other than indirectly). Finally, the number of members who use these services at the 11 credit unions that offer them is extremely low.

A Credit Union *De Minimis* Exemption

CCUA believes the CSA should apply "proportionality" and a "risked-based" policy lenses to national instruments like MI 93-101. These principles are widely used by a range of regulators, including provincial credit union regulators but also the Office of the Superintendent of Financial Institutions (OSFI), the federal market conduct regulator, the Financial Consumer Agency of Canada (FCAC) and the Basel Committee on Banking Supervision (BCBS)[6].

The application of these principles hinges on the idea that "one-size-fits-all" policies harm competition because of their disproportionate effect on smaller institutions like credit unions. Constraints on competition in turn harm the consumer interests that regulatory measures often seek to protect. In this case, the compliance costs of aligning with the proposed instrument could outweigh the benefits of offering these services to members, leading to the withdrawal of these services and possibly a concentration of offerings at larger banks.

[6] For a discussion in a prudential context see: http://www.bis.org/fsi/publ/insights1.htm

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Given these competitive considerations, the application of these principles often translates into some kind of *de minimis* exemption threshold for smaller institutions engaged in less risky activities. With that in mind, CCUA recommends the addition of a *de minimis* exemption in the multilateral instrument for credit unions based on a notional dollar amount threshold. Alternatively, we would urge provincial securities regulators to consider a *de minimis* exemption by drawing on section 45 (part 7), which provides that a regulator or securities regulatory authority may grant an exemption from the instrument in whole or in part subject to applicable conditions or restrictions.

To set the threshold, the CSA could seek inspiration from the Commodity Futures Trading Commission (CFTC), which provides for a registration exemption to "persons" if the swap positions entered into "over the course of the immediately preceding 12 months have an aggregate gross notional amount of no more than $3 billion, subject to a phase in level of an aggregate gross notional amount of no more than $8 billion applied ... and an aggregate gross notional amount of no more than $25 million with regard to swaps in which the counterparty is a 'special entity'."[7]

Conclusion

CCUA is grateful for the opportunity to share its views on NI 93-101. We would be pleased to provide any additional information as required with respect to our comments. Please do not hesitate to contact me at mpigeon@ccua.com or directly by phone at 613-238-6747 x 2310.

Yours truly,

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[7] See https://www.law.cornell.edu/cfr/text/17/1.3.