



Canadian Life
and Health Insurance
Association Inc.

Association canadienne
des compagnies d'assurances
de personnes inc.

June 14, 2012

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

**Canadian Securities Administrators Consultation Paper 91-405 on Derivatives:
End-User Exemption**

The Canadian Life and Health Insurance Association is pleased to provide comments on the Canadian Securities Administrators Consultation Paper 91-405 on Derivatives: End-User Exemption.

Established in 1894, the Canadian Life and Health Insurance Association (CLHIA) is a voluntary trade association that represents the collective interests of its member life and health insurance insurers. The industry, which provides employment to almost 135,000 Canadians and has investments in Canada of \$514 billion, protects more than 26 million

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Canadians through products such as life insurance, annuities, RRSPs, disability insurance and supplementary health plans. It pays benefits of almost \$65 billion a year to Canadians and administers over one-half of Canada's pension plans. Canadian Life insurance companies participate as end-users in Canadian and international over-the-counter derivatives markets.

Although the term "financial institution" is not defined in the Consultation Paper, life insurers are financial institutions pursuant to the definitions provided under their governing legislation (e.g., the Insurance Companies Act, Ontario's Insurance Act), and accordingly it would appear that the end-user exemption is not contemplated to apply to life insurers. We think this exemption should be available to life insurers subject to considerations of systemic risk. It would be helpful for the CSA to provide the policy reasons and rationale for this direction. The life insurance industry would appreciate a definition of the term financial institution to assist with clarifying the meaning in the context of the end-user exemption.

As indicated in our previous letters, it should be noted that the activity of life insurers related to OTC derivatives is substantially different than that of banks. Whereas life insurers are participants in the buy-side of the derivatives market, banks function as the market makers. Requirements should be based on the type of activity which is being undertaken.

The Consultation Paper states that market participants who fall within the category of "large derivatives participants" will not be eligible for the exemption and will be required to meet registration requirements. As a logical extension, consideration needs to be given to what would constitute "large derivatives participants", with the focus on systemic risk.

In this context, the CLHIA believes that the CSA should establish a de minimis level at which the requirements would not apply. We are concerned that, particularly in the case of smaller life insurers, the cost of undertaking OTC derivatives transactions will become so high that it will not be economically feasible to participate in the market. If OTC derivatives are only being used for hedging purposes and are at a level which does not pose any systemic risk then the exemption should be available.

The CLHIA recommends a staged implementation of requirements. Reporting to a trade repository forms a logical first step, whereby market data would become available which would in turn then allow for determining an appropriate threshold of trading at which qualification for using the exemption would apply. Collection of such data will allow for assessing the issue of systemic risk.

As discussed in the Consultation Paper, there are situations where OTC derivative hedging activities are done within one legal entity to hedge business risks of a related affiliated entity or series of legal entities within that affiliated group. The industry agrees



with the Committee that the policy reasons supporting the establishment of the exemption should apply to transactions between affiliated entities but should not be restricted to those situations where each such entity would otherwise meet the eligibility criteria for the exemption. Insurers often arrange OTC transactions with an arm's length entity (e.g. a bank) and then do an internal swap with an affiliate for cash or collateral management or other internal reasons. Such back-to-back internal transactions should not be subject to notice or reporting obligations as the swap with the arm's length counterparty will already have been subject to reporting requirements and this additional data will only distort meaningful information to regulators with respect to marketplace volumes and types of transactions. Such back-to-back internal transactions should be considered exempt from any registration, clearing and capital requirements regardless of whether the parties are financial institutions or large derivatives participants.

The life insurance industry agrees with the Committee's view that a definition of hedging should include traditional concepts of hedging as well as the concept of "mitigation of commercial risk".

The life insurance industry would appreciate receiving more specific details regarding what the end-user exemption will exempt from. For instance, what would happen in the situation where one participant in an OTC derivatives transaction is relying on the exemption but the other is not. In this regard, we would appreciate a further opportunity to comment when more details are available.

As noted in previous submission letters, it is important to maintain a national harmonized regime and for the Canadian derivatives regulatory regime to be harmonized with international jurisdictions.

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

Yours truly,

James Wood
Counsel