



Submission and Comments on CSA Consultation Paper 91-405 Derivatives: End-User Exemption

Submitted to:

**Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Manitoba Securities Commission
New Brunswick Securities Commission
Ontario Securities Commission
Saskatchewan Financial Services Commission**

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Comments on CSA Consultation Paper 91-405

Derivatives: End-User Exemption

Introduction

Concentra Financial Services Association ("Concentra") is Canada's only Retail Association, defined and governed by the *Cooperative Credit Associations Act*. Concentra is regulated by the Office of the Superintendent of Financial Institutions ("OSFI") through application of the Regulations of the *Trust and Loan Companies Act*.

Concentra is a small national financial institution offering a variety of services to credit unions across the country, with the exception of Quebec. Concentra has assets of about \$6 billion, primarily consisting of residential and commercial mortgages and securities. These services include loan syndication and securitization, deposits, foreign exchange and financial consulting. Concentra will deal directly with credit union members only when requested by the credit union, in such areas as leasing and trust services.

Derivative activity

For its own balance sheet, Concentra uses a variety of derivatives as a risk mitigation tool. Specifically, the company uses interest rate derivatives to manage interest rate risk exposure on the balance sheet, foreign exchange and cross currency swaps to manage foreign currency exposure on the balance sheet, and interest rate derivatives to manage risk within pipeline of the Canada Mortgage Bond program.

Concentra also supports credit unions in their access to financial derivatives. Individual credit unions do not have the business volume to be supported by the major derivative suppliers in the country. Concentra operates as an intermediary to facilitate the risk mitigation activities of credit unions. The types of transactions are similar to those conducted by Concentra. In addition, equity derivatives are used to hedge specific deposit products that are offered to members (such as index linked deposits)

The activity of Concentra with respect to derivatives is reviewed extensively by internal and external auditors as well as by OSFI. Derivatives have not been classified as "trading" for financial reporting purposes. In addition, Concentra holds capital against risks associated with derivatives through the capital adequacy requirements of OSFI. Concentra has specific arrangements with a number of counterparties for the acquisition of derivatives, with collateral requirements as necessary

Specific comments

Criteria considered for eligibility under the end user exemption as outlined in the Consultation Paper are:

i) trading for own account, not a registrant or affiliate of a registrant;

ii) not a financial institution;

iii) hedging to mitigate commercial risks related to the operation of a market participant's business; or

iv) centralized risk management and intragroup trading considerations.

Concentra believes that this broad categorization lumps all financial institutions into a category that is inappropriate for the nature of the activities being undertaken. As identified above, Concentra uses derivative transaction as a risk mitigation tool, not as a trader. The potentially onerous reporting and compliance regime will add process to a currently effective program. In addition, achieving the unique structures required to effectively mitigate risk may become more difficult.

Ultimately, without an exemption, small financial institutions such as Concentra may be exposed to greater risk potentially through alternative efforts at risk mitigation. The activities in intermediation are directly flowing through derivative transactions to credit unions to facilitate their risk management.

We believe that these activities are well documented and controlled, therefore do not require an additional level of complexity added to the process.

As a final point, similar derivative legislation is currently being implemented in the United States under the *Dodd-Frank Wall Street Reform and Consumer Protection Act*. Under the proposed rules set by the Commodity Futures Trading Commission, small banks and credit unions with assets of \$10 billion or less would be eligible for exemption. Concentra respectfully suggests these proposed rules can provide guidance to Canadian Securities Administrators to define what would constitute a small financial institution that could be exempted without impacting the OTC derivatives markets in Canada. Enacting similar rules as those proposed by our American counterparts would have the additional benefit of providing consistency and fairness across the industry.

Conclusion

Concentra supports end user exemption being applied to small financial institutions, including those acting as market intermediaries for smaller organizations that do not have access to the OTC market. Concentra supports the need to have board approval for the use of OTC derivatives for risk management purposes only and the requirement to have transparency in the reporting, including disclosure of activity to Asset Liability Committee.



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