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June 13, 2012

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

John Stevenson, Secretary  
Ontario Securities Commission  
20 Queen Street West, Suite 1900, Box 55  
Toronto, ON M5H 3S8

Me Anne-Marie Beaudoin  
Corporate Secretary  
Autorité des marchés financiers  
800, square Victoria, 22<sup>e</sup> étage  
C.P. 246, tour de la Bourse  
Montréal (Québec) H4Z 1G3

Dear Sirs / Madames:

**RE: CSA Consultation Paper 91-405 Derivatives: End-User Exemption**

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Thank you for the opportunity to provide comments to the Canadian Securities Administrators ("CSA") regarding Consultation Paper 91-405 Derivatives: End-User Exemption ("CP 91-405") related to the implementation of Over-the-Counter ("OTC") derivatives end-user exemptions from proposed regulatory requirements governing registration, trading, clearing, margin, capital and collateral.

Fidelity Investments Canada ULC ("Fidelity Canada") is a fund management company in Canada and part of the Fidelity Investments organization in Boston ("Fidelity Investments"), one of the world's largest financial services providers. Fidelity Canada manages a total of \$66 billion in mutual funds and institutional assets (the "Funds"). It offers approximately 140 mutual funds and pooled funds to Canadian investors.

Fidelity Canada's use of OTC derivatives currently includes currency forwards to hedge currency risk in certain Funds, interest rate swaps for the purpose of managing fixed income portfolio duration, and customized forwards in certain funds managed by Fidelity Canada.

Fidelity Canada supports the Canadian Securities Administrators Derivatives Committee's (the "Committee") efforts to allow for end user exemptions from registration and other regulatory requirements. As noted in previous Fidelity Canada submissions, Fidelity Canada is concerned about the impact of the Committee's proposals on the cost of managing Funds that use OTC derivatives, especially where such use is fundamental to the investment objectives and strategies of a Fund. We look forward to more detailed information related to the regulatory framework and the application of end user exemptions within that framework in order to assess how the end user exemption might mitigate the cost of using OTC derivatives in Canadian investment funds.

Fidelity Canada's responses to the questions in CP 91-405 are noted below:

**Question 1: Do reporting obligations create any barriers to participation in the derivatives market that would be unique to end users or a category of end users? Please provide a description of the potential issues that end users may face.**

As noted by the Committee in Consultation Paper 91-402, we agree that reporting OTC derivative transaction data to trade repositories will greatly improve market transparency and is an essential component of derivative market reform. We also agree that a requirement to report trades to a trade repository will assist regulators in monitoring the effectiveness of an end user exemption, and provide important information to regulators for monitoring improper conduct. However, to the extent market participants would be required to implement new operational processes and controls to facilitate reporting, and/or financially support the creation and maintenance of a domestic or international trade repository, we encourage the Committee to consider options that respond to the need to minimize these costs.

For end users, internal costs may include new system development to ensure transaction data is reported in accordance with international standards, establishing processes to report continuation data throughout the life of a contract, and allocating personnel resource to effectively manage and oversee the reporting process. If these reporting responsibilities reside with financial intermediaries that have already established an operational infrastructure capable of providing reporting and have systems and procedures that are scalable, these costs may be minimized, however the incremental cost of reporting OTC derivative trades on behalf of end users are likely to be passed in whole or in part to the end user. We recognize that reporting obligations will result in additional cost, but are sensitive to how these costs may present a barrier to participation in the OTC derivative market.

**Question 2: Are the end user eligibility criteria proposed by the Committee appropriate?**

We are supportive of the Committee's recommendation that criteria be developed that provide for end-user exemptions from registration and other regulatory requirements. In addition, we support the establishment of eligibility criteria that are consistent with those in foreign jurisdictions on the basis that consistency might facilitate access to those markets for Canadian market participants. We understand the intent of developing these criteria is to establish a regulatory framework that allows for the effective management of systemic risk without impeding

market participants' ability to effectively manage specific business risks using OTC derivatives. As such, the criteria are generally appropriate, however, we encourage the Committee to consider how these criteria might apply to Canadian investment funds that may themselves qualify for an end user exemption even though the investment fund manager or advisor may not under the currently proposed criteria.

For example, certain Fidelity Canada Funds use forward contracts to hedge currency risk and this ongoing strategy is a fundamental component of the mandate of those Funds. The use of currency forwards is intended to mitigate the commercial risk posed by fluctuations in foreign currency prices and their use is consistent with the Committee on Payment and Settlement Systems of the Bank of International Settlements and the technical Committee of International Organization of Securities Commissions' definition of "hedge or hedging". Based on the Committee's proposed criteria for end user exemption, we would consider that these Funds should be exempt. However, it is unclear how the proposed exemption would be applied to Canadian investment funds. We are encouraged by the Committee's comment that it is possible some financial institutions or other market participants may not be required to meet all of the proposed regulatory requirements, but are concerned that these Funds may not be considered in-scope of the end user exemption proposal.

We encourage the Committee's continuing efforts to develop clear guidance concerning what specific activities will qualify as "mitigating commercial risks related to the operation of the business". Specifically, the concept of "reducing the risk of loss" should be explored in more detail to determine whether the use of OTC derivatives to mitigate transaction costs and liquidity constraints in an investment fund would qualify as transactions subject to the end user exemption criteria. For example, investment funds may use OTC derivatives to tactically manage short term market exposure in a prudent and non-leveraged manner under National Instrument 81-102 ("NI 81-102") to mitigate trading costs associated with trading securities held in a portfolio. While not technically a "hedge" under the proposed definition, such use is arguably not "speculative" in nature and does assist in reducing the "risk of loss". We look forward to discussing the results of the Committee's ongoing development of clear guidance concerning what specific activities will qualify as "mitigating commercial risks related to the operation of the business".

**Question 3: Should alternate or additional criteria be considered?**

We encourage the Committee to consider applying the end user exemption to Canadian mutual funds on the basis that they are subject to NI 81-102 provisions that prohibit the use of leverage, impose limits on counterparty exposure, and prescriptively govern the credit quality of permitted counterparties. We consider that the use of OTC derivatives in Canadian mutual funds poses little systemic risk and that extending the end user exemption to Canadian mutual funds will potentially reduce the cost to the Funds of using OTC derivatives without causing a meaningful increase in systemic risk.

**Question 4: Are the Committee's recommendations to exclude the specified end user eligibility criteria from consideration appropriate?**

We agree that in the absence of comprehensive market data, setting a *de minimus* threshold for determining end user exemption eligibility would not be appropriate. We would, however, encourage the Committee to further develop its views on sector specific exemptions relative to the use of OTC derivatives in Canadian mutual funds. As noted above, we support the notion that all OTC derivative trades are subject to reporting requirements for the purpose of facilitating regulatory monitoring, but would like the Committee to consider a “sector specific” end user exemption for Canadian mutual funds subject to NI 81-102. We also agree that the end user exemption would be unduly restrictive if it required eligible end users to use standardized contracts or clearing where available.

**Question 5: Is the Committee’s proposal that the market participant itself determine its qualification for an exemption and provide notice to the regulator of its intention to rely on the exemption appropriate?**

We agree that of the proposals presented, allowing a market participant itself to determine whether it qualifies for an end user exemption and provide notice to the regulator of its intention to rely on the exemption is the most reasonable option. Under this self-assessment model we encourage the Committee to ensure that the criteria under which firms are required to make the eligibility determination are clear.

**Question 6: Is the proposed process to be followed by eligible end users wishing to rely on the exemption appropriate?**

We agree with the Committee’s proposal that market participants provide regulators with a notice of intent to rely on the end user exemption as a one time filing applicable to all provinces and territories, that material changes should trigger additional notice, and that the filing be made electronically. We also consider it appropriate that market participants be responsible for maintaining books and records to demonstrate it meets the legal requirements of an end user exemption.

**Question 7: Is the Committee’s proposal to require board of directors’ approval of the use of OTC derivatives as a risk management tool to demonstrate hedging compliance appropriate for non-registrant entities?**

We agree that it is appropriate for market participants to obtain Board approval should they wish to apply for the end user exemption, and that market participant Boards should review and approve policies and procedures that govern the use of OTC derivatives at their firm. We are also in favour of periodic management reporting to the Board that demonstrates compliance with end user exemption criteria and approved policies and procedures. We consider this oversight process should not be conducted with respect to each trade, but that policies and procedures should be approved as “standing instructions” with respect to OTC derivatives use and reliance on the end user exemption. Any proposed material change to the standing instruction should require Board review and approval prior to the execution of a new strategy to ensure the application of the end user exemption is appropriate.

We thank you for the opportunity to comment on these matters. As always, we are more than willing to meet with you to discuss any of our comments.

Yours truly,

A handwritten signature in blue ink, appearing to read "Tom Phillips".

Tom Phillips  
Manager, Investment Compliance

c.c. Rob Strickland, President  
W. Sian Burgess, Senior Vice-President, Head of Legal and Compliance, Canada  
Fidae Abbas, Vice-President, Compliance, Canada