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VIA EMAIL: [consultation-en-cours@lautorite.qc.ca](mailto:consultation-en-cours@lautorite.qc.ca), [jstevenson@osc.gov.on.ca](mailto:jstevenson@osc.gov.on.ca)

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

c/o:

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

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

**Re: Canadian Securities Administrators (“CSA”) Consultation Paper 91-403 –  
Derivatives: Surveillance and Enforcement**

Dear Members of the CSA Derivatives Committee:

The Canadian Electricity Association (“CEA”) is pleased to provide the following comments on the CSA Derivatives Committee’s (“Committee”) Consultation Paper 91-403, entitled *Derivatives: Surveillance and Enforcement* (“CP 91-403”). CEA submitted comments on the Committee’s previous consultation paper regarding trade repositories – Consultation Paper 91-402, entitled *Derivatives: Trade Repositories* (“CP 91-402”)<sup>1</sup> – and appreciates the opportunity to continue engaging the Committee in the evolving formation of its proposals for a regulatory framework for the over-the-counter (“OTC”) derivatives marketplace in Canada.

**I. Introduction**

CEA is the national forum and voice of the evolving electricity business in Canada. CEA members generate, transmit and distribute electrical energy to industrial, commercial, residential and institutional customers across Canada every day. From vertically integrated electric utilities,

<sup>1</sup> CEA’s comments are accessible at the following link:

[http://www.osc.gov.on.ca/documents/en/Investors/com\\_20110912\\_91-402\\_guimond.pdf](http://www.osc.gov.on.ca/documents/en/Investors/com_20110912_91-402_guimond.pdf)

to power marketers, to the manufacturers and suppliers of materials, technology and services that keep the industry running smoothly – all are represented by this national industry association.

As detailed in CEA's comments on CP 91-402, CEA members have a significant interest in the Committee's ongoing effort to map out an OTC regulatory framework. OTC derivatives serve as one of the many valuable tools available to CEA members to manage the commodity and commercial risks associated with their core business of providing a reliable and affordable supply of electricity to consumers across Canada. Those CEA members which engage in OTC derivative transactions do so primarily for purposes of hedging these risks, thereby insulating customers from price volatility in energy markets. CEA wishes to reinforce its earlier comments that, as commercial hedging end-users and non-financial entities, CEA members do not engage in the OTC derivative market in a manner which poses sufficient systemic risk concerns. As such, CEA strongly encourages CSA members to bear in mind at each phase throughout this consultation process how regulation of the OTC marketplace in Canada will impact end-users of commodity and energy derivatives.

It is from the vantage point of the commercial hedging end-user that CEA members offer the following comments on the CSA's proposals for surveillance, monitoring and enforcement in the OTC derivatives market.

## **II. General Comments**

CEA notes that CP 91-403 calls for further study by provincial market regulators on a host of important issues which will be fundamental to the establishment and operation of a comprehensive surveillance system for OTC derivatives markets. These issues include essential operational issues such as which entity or entities will be tasked with surveillance responsibilities, and what resources, expertise and analytical capabilities are necessary to conduct OTC market surveillance.

The numerous instances in which the need for additional analysis is highlighted in CP 91-403 suggest that CSA members' efforts to identify specific, clear, common objectives for market surveillance purposes remain at an incipient stage. As a general matter, CEA would caution the Committee against moving too far forward with its subsequent proposals before these further studies are conducted and published for consultation with stakeholders.

The proposed regulation of the complex and dynamic OTC derivatives marketplace is an enterprise that warrants a well-planned strategy, based on robust and extensive background information, with objectives – and measures for reaching those objectives – clearly defined at the onset. The issues examined in the studies recommended by the Committee may help shape and enhance the proposals contemplated for later consultation papers. CEA does not believe that it will serve the interests of any participant engaged in this consultation process for the next round of proposals to pre-empt studies aimed at answering core questions around surveillance and monitoring issues, only for the Committee to discover that it would have re-formulated certain proposals based on the results of these studies.



Accordingly, CEA respectfully urges the Committee to assess whether the publication of further consultation papers – as per the Committee’s current schedule<sup>2</sup> – prior to the completion of these studies identified as necessary by the Committee risks compromising the overall efficiency of this consultation process.

### **III. Specific Comments**

#### **2. Surveillance and Monitoring**

CEA requests clarification regarding the precise OTC market information to which CSA members believe they must have access in order to achieve their surveillance objectives.

For example, CEA notes language in paragraph 2 of subsection (b) in this section, regarding *Monitoring Participant Positions*, which reads as follows:

“[T]he Committee recommends that provincial market regulators, in coordination with other key Canadian financial market regulators, obtain data relating to derivatives positions held by these participants to understand the risks to those participants, the market and the Canadian economy. This data will include transaction information *as well as information provided by the market participants themselves* [emphasis added].”<sup>3</sup>

However, in the ensuing discussion on access to data in subsection (c), *Management of Data*, the Committee states the following:

“Trade repositories would make transactional and aggregated data available to regulatory authorities on a routine and per-request basis.”<sup>4</sup>

Based on the language in subsection (c) and on the general discussion in CP 91-402, it is CEA’s understanding that market participants will fulfill data reporting requirements through direct reports to a trade repository. CP 91-402 does not expressly contemplate direct reporting of transaction data from market participants to provincial regulators. Rather, the trade repository is viewed as serving as the appropriate intermediary through which all relevant data from market participants passes to the applicable provincial authorities.

In CP 91-402, the Committee identifies three categories of information which it anticipates CSA members will require market participants to submit to trade repositories: creation data, continuation data and valuation data.<sup>5</sup> Beyond these three data sets, CEA is unsure as to what additional information “provided by the market participants themselves” CSA members are interested in receiving for surveillance purposes.

In addition, with respect to the applicable language in paragraph 2 of subsection (b) cited above, CEA requests clarity regarding the identity of the “other key Canadian financial market

<sup>2</sup> [http://www.osc.gov.on.ca/en/SecuritiesLaw\\_proposed\\_index.htm](http://www.osc.gov.on.ca/en/SecuritiesLaw_proposed_index.htm) [Accessed: January 25, 2012]

<sup>3</sup> CP 91-403, p. 9.

<sup>4</sup> *Ibid*, p. 10.

<sup>5</sup> CP 91-402, p. 24.



regulators” to which the paragraph refers and whether requirements for OTC derivatives users to report data to these institutions are or will be contemplated.

CEA believes the conflicting and vague language in these subsections serves as a reminder of the need for vigilance on the Committee’s part in avoiding the imposition of potentially duplicative and onerous reporting requirements on OTC users. More broadly, this language further highlights the need for CSA members to reach consensus on what market information they believe is essential to reaching a robust level of surveillance and monitoring, before proceeding to subsequent phases of the Committee’s consultation process which will rely on a firm understanding of data to be obtained and analyzed.

### **3. Market Conduct Rules**

#### (e) Record-Keeping and Audit Trail Requirements

CEA also notes with interest the Committee’s proposal, in paragraph 2 of this subsection, to impose record-keeping requirements on “derivatives dealers, derivatives advisers and significant derivatives participants” under the new OTC regulatory regime.

As an initial matter, CEA trusts that the Committee will provide in the future – perhaps in conjunction with its consultation paper on registration – a clear definition of “significant derivatives participant.” Such definition will provide clarity to OTC users regarding the level of participation in the OTC derivatives market which CSA members regard as posing systemic risk and ought to assist in differentiating the compliance burden that is appropriate for entities engaged in OTC transactions based on their respective risk profiles.

CEA acknowledges the Committee’s intention to further address record-keeping requirements in a subsequent consultation paper. CEA strongly encourages the Committee to carefully evaluate whether imposing uniform requirements on all OTC derivative users (i.e. financial and non-financial entities alike) represents a measured, cost-effective regulatory approach, and to consider differentiated requirements based on transactions, product types and an entity’s risk profile. CEA would caution that the simple extension of existing record-keeping requirements under provincial securities legislation to all OTC derivatives users may have the adverse effect of imposing disproportionate burdens on commercial hedging end-users. CEA urges CSA members to bear this potential outcome in mind as they assess the feasibility and merit of this proposed course of action.

#### (h) Abuse of exemptions

In step with CEA’s comments on CP 91-402, CEA supports the Committee’s signaled intention to implement certain exemptions from new mandatory requirements – such as clearing, margin or collateral requirements – for certain types of transactions and for defined categories of end-users that trade in OTC derivatives. CEA agrees that robust provisions are warranted to guard against exemption abuse, such as the misrepresentation of an entity’s eligibility for qualification as an end-user. CEA looks forward to reviewing and commenting on the Committee’s forthcoming consultation paper on end-user exemptions.



### (i) Position Limits

In view of the substantial further study which the Committee intends to conduct on a host of issues relevant to surveillance, CEA supports the Committee's decision to refrain from proposing draft rules on position limits at this time. CEA believes that, absent a more crystallized vision of the necessary structures for OTC regulation, a discussion around the establishment of position limits would be premature.

## IV. Conclusion

CEA continues to support the important objective of achieving transparency and stability in the OTC derivative marketplace in Canada. CEA appreciates the opportunity to provide feedback on CP 91-403 and respectfully requests that the CSA consider the comments set forth herein. We look forward to engaging the CSA on future proposals around the formation of a comprehensive framework for OTC regulation in Canada.

Please do not hesitate to contact the undersigned if CEA can be of any further assistance.

Respectfully submitted,

/s/ Francis Bradley

Francis Bradley  
Vice President, Policy Development  
Canadian Electricity Association  
(613) 230-5027  
[bradley@electricity.ca](mailto:bradley@electricity.ca)

/s/ Patrick Brown

Patrick Brown  
Director, U.S. Affairs  
Canadian Electricity Association  
(613) 627-4124  
[brown@electricity.ca](mailto:brown@electricity.ca)

