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January 23, 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 91-403 Derivatives: Surveillance and Enforcement**

Thank you for the opportunity to provide comments to the Canadian Securities Administrators ("CSA") Consultation Paper 91-403 Derivatives: Surveillance and Enforcement ("CP 91-403") related to the surveillance, monitoring and enforcement of Over-the-Counter ("OTC") derivatives markets in Canada.

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 \$64 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 the Fidelity Corporate Bond Capital Yield Class and the Fidelity Premium Fixed Income Capital Yield Private Pool ("Capital Yield Funds"). The Capital Yield Funds invest primarily in equity securities issued by Canadian corporations and

enter into forward contracts in order to hedge their exposure to the equities and provide the Fund with a return based on the performance of a Canadian fixed income fund managed by Fidelity Canada.

Fidelity Canada generally supports the views of the Canadian Securities Administrators Derivatives Committee (the “Committee”) and the Committee’s recommendations relative to ensuring provincial market regulators effectively monitor, detect, deter and enforce against improper market conduct in the OTC derivatives market.

Fidelity Canada’s responses to the CSA’s views and recommendations noted in CP 91-403 are noted below:

### **Surveillance and Monitoring Costs**

We agree that OTC derivative market transparency is essential to ensuring provincial market regulators are able to detect improper market conduct, systemic risks, problematic positions and other activities that have the potential to affect the integrity of capital markets. The importance of transparency was highlighted in Consultation Paper 91-402 *Derivatives: Trade Repositories*, and it is evident in CP 91-403 that even with the establishment of a functioning trade repository, provincial market regulators face considerable challenges with respect to obtaining a view of domestic and international cross-market and cross-product interconnectivity. As noted in CP 91-403, there will be various costs associated with the implementation and management of a comprehensive surveillance system including the development of an electronic system which can analyze cross-market and cross-product data, the development of a system capable of storing and archiving data, IT maintenance and support, the development of surveillance methodologies and increases in staff resources. Due to the distinct sources of market information and oversight procedures currently in place in Canada, the cost of coordinating surveillance and monitoring activities may be prohibitive relative to the benefits accrued.

As an OTC derivative market participant, we are concerned that the implementation of the proposed surveillance approach will result in increased costs that may be passed on to our Funds and that such cost increases may render certain product features economically unviable for certain Funds. This may reduce Fidelity Canada’s ability to provide the investing public with products that suit their specific needs (e.g. by altering the cost structures of products that engage in currency hedging using forward contracts such products may not be viable). As such, we recommend that throughout the development and implementation of surveillance and monitoring programs for OTC derivatives markets provincial market regulators make a concerted effort to minimize costs.

### **Monitoring Participant Positions**

At the root of the CSA’s proposals is the notion that systemic risks associated with the use of OTC derivatives cannot be identified or governed by market participants and we agree that monitoring such risk falls within the purview of provincial market regulators. As such we support the notion that provincial market regulators establish a means to identify and quantify systemic risk and any associated imbalance in the market. However, even if provincial market regulators had access to information sufficient to perform this assessment, it is unclear what course of action would be taken by regulators to mitigate the risk. As provincial market regulators work to establish monitoring procedures, we encourage discussion on how they define a “key participant” in the OTC derivatives market as well as what sort of actions will be taken to manage systemic risk, including whether there will be derivative position limits imposed,

whether additional oversight processes will be implemented, and whether there will be more stringent capital, margin or collateral requirements imposed on market participants.

### **Cooperative Information Sharing**

As noted in CP 91-403, due to the relatively small size of the OTC derivatives trade in Canada relative to the global trade, it is important that provincial market regulators establish collaborative arrangements with international regulatory bodies to obtain a complete view of the market and any pooled systemic risk. Assuming provincial market regulators are able to negotiate effective information sharing and confidentiality agreements among themselves and with international counterparts, we encourage the inclusion of reporting standards to ensure that surveillance, monitoring and enforcement activities in Canada are not delayed due to a reluctance of foreign regulatory authorities to disseminate information about their market or market participants. In the event required information is not made available to effectively enforce Canadian rules, the costs associated with the implementation of a record keeping and monitoring system in Canada may not generate the expected value. It is also important for provincial market regulators to ensure that they have at their disposal effective remedies should a foreign jurisdiction not be willing to disclose information necessary to identifying systemic risk in Canada.

At the same time, the confidentiality of information related to derivatives trading and positions taken by Canadian market participants is essential to maintaining the integrity of the Canadian market and the effectiveness of the OTC derivative strategies employed by Canadian market participants. We thus encourage provincial market regulators to ensure that interprovincial and international agreements to share information include strict provisions on the availability of OTC derivative trading, positions, and Canadian market participants.

We agree there are significant complexities associated with both accessing information and making information available across multiple jurisdictions, but we also acknowledge that in order to identify and mitigate systemic risk, such information sharing is crucial.

### **Cooperative Surveillance, Monitoring and Enforcement**

We support the CSA's recommendation that provincial market regulators work collaboratively toward a surveillance, monitoring and enforcement framework that is consistent across Canada and, if possible, internationally, in order to minimize market participant compliance costs.

We also agree with the CSA's recommendation that provincial market regulators consider applying existing market principles to the OTC derivatives market, including those related to market manipulation and fraud, misrepresentations, abusive trading practices, insider trading, etc. However, in light of the complexities of engaging in monitoring the OTC derivative market, including doing so on a cross-market and cross-product basis as well as in light of new requirements related to centralized trading and clearing facilities, mandatory reporting, and new capital and collateral requirements, we encourage provincial market regulators to ensure the implementation of these principles is tailored to the unique attributes and needs of the market. We thank you for the opportunity to comment on the proposed amendments. As always, we are more than willing to meet with you to discuss any of our comments.

Yours truly,



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