ANNEX A

COMMENT SUMMARY AND CSA RESPONSES

Section Reference	**Issue/Comment**	**Response**
General Comments	<u>Harmonization</u> A number of commenters raised concerns about a possible lack of harmonization across provinces in the implementation of the Clearing Rule and in the determination of derivatives to be subject to mandatory clearing.	Change made. We note that the Committee has now opted to develop a national instrument, given its intention that the substance of the rules be the same across jurisdictions, and that market participants and derivative products will receive the same treatment across Canada, both in terms of participants (similar exemptions) and of products (same determinations) included. See *Determination of mandatory clearable derivatives* above.
	<u>Implementation</u> A commenter requested greater clarity regarding the intended timing of implementation and application of the Clearing Rule. Another commenter recommended that the local provincial regulators give sufficient time to counterparties to get set up with their clearing intermediaries and agents.	No change. The committee would like to see the rule in place by Q4 2015 or Q1 2016. We note that a requirement to clear would not be triggered until a proposed determination has been published for comment and a final determination made. See *Phase-in of the requirement to clear a mandatory clearable derivative* above.
	<u>Determination</u> Four commenters were concerned about the harmonization, within Canada and at the international level, of derivatives subject to mandatory clearing. Three commenters proposed a joint determination process for the local provincial regulators. Three commenters suggested types or classes of derivatives that should or should not be mandated for clearing, and one	No change. See *Determination of mandatory clearable derivatives* above. We also note that the existence of master agreements or short form confirmations is a factor considered in evaluating the level of standardization of a derivative.

	commenter discussed additional factors to consider when making a determination. Two commenters suggested that a "top-down approach" whereby local provincial regulators assess what types of products and transactions contribute to systemic risk in the market and determine, based on their analysis, that certain products are "clearable derivatives", should be considered in addition to the bottom-up approach. Another commenter supported an approach whereby a regulator cannot mandate that a clearing agency clears a particular clearable derivative. Finally, five commenters requested that regulators provide advance notice or mandatory consultations with the industry before mandating a derivative or class of derivatives for clearing.	
	Scope A commenter submitted that OTC derivative transactions involving physical commodities such as OTC natural gas commodity hedging transactions should not be classified as derivatives per the Draft Model Rule's definitions and therefore should not be subject to the pending derivatives legislation.	No change. We note that it is the intention of the Committee that the determinations to be made will not include derivatives that are outside the scope of the local *Derivatives: Product Determination*[1] rules.
S. 1 – Definitions: Local Counterparty	A commenter pointed out that the local counterparty definition in TR Rules differs from the local counterparty definition in the Draft Model Rule.	No change. We note that the inclusion of registrants in the local counterparty definition of the Clearing Rule would result in requiring foreign registrants to

[1] Manitoba Securities Commission Rule 91-506 *Derivatives: Product Determination*, Ontario Securities Commission Rule 91-506 *Derivatives: Product Determination*, Québec *Regulation 91-506 Respecting Derivatives Determination* and Proposed Multilateral Instrument 91-101 *Derivatives: Product Determination* (the **Scope Rules**).

		clear even when there is no local counterparties involved in a transaction.
	A number of commenters requested additional guidance on concepts such as "head office", "principal place of business" and "affiliate" or, more specifically, what is meant by "responsible for the liabilities of that affiliated party". Another commenter suggested cross-referencing the definition of local counterparty found in the Policy Statement of the TR Rules.	No change. We note that these are longstanding legal concepts.
	A commenter pointed out that the definition of local counterparty brings into the clearing requirements numerous counterparties that conduct no business and, in particular, do not carry out any derivative trading activities in Canada, such as companies organized under a province law but which have no actual presence or business in Canada.	No change. We note that a local provincial regulator may exempt entities or groups of entities in its jurisdiction.
S. 1 – Definitions: Financial Entity	A commenter pointed out that former paragraph 1(g) reference to former paragraph 1(f) would capture any entity anywhere in the world that might potentially be subject to registration as a derivatives dealer in Canada. The practical effect of this is that any such party transacting with a local counterparty that is itself a financial entity may be subject to mandatory clearing requirements in Canada regardless of whether the transaction is eligible for a clearing exemption in such party's own jurisdiction. Another commenter suggested that a local counterparty has	No change. See *Determination of mandatory clearable derivatives* above. We note that the local provincial regulators intend to adopt a "stricter rule applies" principle in case of cross-border discrepancies. As a result, when a foreign party transacts with a local counterparty in a derivative that is subject to mandatory clearing under the Clearing Rule, the transaction must be cleared even if an exemption exists in the foreign party's jurisdiction. We also note that the Committee continues to monitor the development of cross-border guidance with respect to

	satisfied its clearing requirement in respect of a transaction if the counterparty to that transaction is not a local counterparty and, if under the applicable laws of the foreign jurisdiction, such transaction is exempt from clearing because the counterparty qualifies for an exemption.	substituted compliance on clearing requirements.
	A number of commenters have requested more clarity on the upcoming registration regime, or to wait until the regime is in place before mandating derivatives to be cleared. Moreover, a number of commenters expressed concern with the inclusion of certain entities in the definition of financial entity, such as pension funds, investment funds (mortgage investment entities, private equity funds and venture capital funds) and entities registered or exempt from registration.	No change. See *Phase-in of the requirement to clear a mandatory clearable derivative* above. We note that the phase-in approach to the clearing requirement will allow the local provincial regulators to provide more clarity on the developing derivatives registration regime, and to use trade repository data to investigate whether thresholds or carve-outs are appropriate for certain types of entities.
	A commenter suggested that, in former paragraph (g), reference should also be made to entities that would be regulated "or exempted from regulation" under the applicable legislation of Canada or the applicable local jurisdiction to conform to former paragraph (f). The commenter further suggested that the statement "had it been organized in Canada or the applicable local jurisdiction" is not necessary.	Change made. See revised section 1. We note that entities exempted from registration are included in the financial entity definition. See *Phase-in of the requirement to clear a mandatory clearable derivative* above.
S. 1 – Definitions: Transaction	Three commenters proposed that trades which reduce risk, such as compression replacement trades, terminations, compression amended trades (partial unwinds) and certain risk rebalancing	No change. We note that the Committee will continue to monitor international regulatory developments with regards to trade compression.

	trades resulting from post-trade risk reduction services should not trigger the clearing requirement.	
	A commenter pointed out that it would be beneficial to have an objective test to determine what is considered to be a "large change".	No change. We note that the Committee considers that the proposed approach provides flexibility as an entity should be able to establish subjectively whether a transaction was amended with the sole purpose of avoiding the central clearing requirement.
Former S. 3 – Interpretation of hedge or mitigation of commercial risk	A number of commenters have requested additional guidance on the concepts of "hedging" and "mitigating commercial risk", and how these differ from "speculation". Commenters also suggested that the Committee adopt a flexible approach to these concepts given the wide variety of derivatives, potential end-users, and hedging strategies to which the Clearing Rule will apply. Another commenter encouraged the recognition of derivatives, which satisfy the requirements under IFRS or U.S. GAAP to be accounted for as hedges, as being held for the purpose of hedging or mitigating commercial risk.	No change. We note that the Committee considers that the proposed approach provides flexibility and legal certainty, and that the Clearing CP provides sufficient guidance on the concepts of "hedging" and "mitigating commercial risk". Additional guidance may be published once compliance with the Clearing Rule is assessed. We also note that hedges meeting the stricter accounting standards should be sufficient to meet the conditions of the end-user exemption.
	A number of commenters requested additional or revised guidance with regards to the interpretation of commercial risk or a definition for the terms "closely correlated" and "highly effective".	Changes made. See revised section 4 on Interpretation of hedge or mitigation of commercial risk.
	A number of commenters pointed out that the list of risks in former paragraphs 3(a)(i) and (ii) may not be exhaustive.	Changes made. We note that the amendments brought to paragraphs 4(1)(a) and (b) are consistent with the definition of Derivatives in the *Securities Act* (Ontario).

	A commenter suggested that the addition of "incurring in the normal course of its business" at the end of former paragraph 3(a)(i) may be problematic as companies develop new risk management strategies as they enter into new lines of business and new commercial arrangements.	No change. We note that new activities occur in the normal course of business. Entities can therefore use the end-user exemption as long as the conditions are met.
	Two commenters stated that they enter into commodity derivatives trading with their customers as part of their core business and are required to hedge these transactions. However, given that the transactions with their customers are not held for the purpose of hedging or mitigating commercial risk, they cannot benefit from the end-user exemption (see former paragraph 3(b)(ii)). They argued that former paragraph 3(b)(ii) should be modified so that the ineligibility applies only where the party concerned is hedging in its capacity as an intermediary or market-maker in derivatives, rather than hedging to mitigate a commercial risk of another kind.	No change. We note that the end-user exemption specifically targets transactions that are entered into to hedge or mitigate a commercial risk incurred by an eligible entity.
Former subsection 4(1) – Duty to submit for clearing	Two commenters pointed out that there may not be sufficient time to clear a transaction before the end of the day if that transaction is executed shortly before the clearing agency closes.	No change. We note that this issue should not materialize where straight-through processing is implemented. The Committee will monitor the implementation of the rule and may provide further guidance if needed.
	A commenter pointed out that technically, the "transaction" is not submitted for clearing. If the transaction has the required features, then the clearer submits the deal terms and a new transaction with the clearing	No change. We note that the Committee believes that the Clearing Rule provides sufficient clarity as currently drafted.

	agency is created. The contract between the original parties no longer exists.	
Former subsection 4(2) – Duty to submit for clearing: substituted compliance	Two commenters suggested to broaden the concept of substituted compliance such that the clearing requirement would be satisfied if the transaction was submitted for clearing, pursuant to the laws of another Canadian jurisdiction or the laws of an approved foreign jurisdiction, to a clearing agency recognized in that jurisdiction.	Partial change made. Substituted compliance was added for a local counterparty in a reliant jurisdiction if the transaction is submitted for clearing to a regulated clearing agency of another jurisdiction of Canada. See *Determination of mandatory clearable derivatives* above. We note that the Committee continues to monitor the development of cross-border guidance with respect to substituted compliance on clearing requirements.
Former S. 5 – Notification	Three commenters were concerned with the operational consequences of considering a transaction to be void *ab initio* if it is rejected for clearing by the clearing agency.	Changes made. See revised Section 7 of the Policy Statement. The guidance now refers to the rules of the clearing agencies and to the legal arrangements governing indirect clearing in place with regards to the rejection of transactions.
Former S. 7 – End-user exemption	A number of commenters pointed out that the end-user exemption should not require a formal agency relationship.	Change made. The reference to "agent" has been removed from former paragraph 7(2)(a).
	A number of commenters requested precisions on the end-user exemption: • Are both the end-user exemption and the intragroup exemption available for intragroup transactions? • Can an entity self-exempt on the basis that it is not a financial entity and is undertaking transactions to hedge or mitigate risk? • In the event that both counterparties are not financial entities, is it	No change. We note that: • Both the end-user exemption and the intragroup exemption are available for intragroup transactions unless the entity seeking exemption is a financial entity (cannot use the end-user exemption). • It is the responsibility of the entity seeking to be exempted to determine whether the exemption applies to its transactions.

	sufficient that only one party satisfies the requirement under former paragraph 7(1)(b)?	• In the event that both counterparties are not financial entities, it is sufficient that only one party satisfies the requirement under paragraph 9(1)(b).
	A number of commenters have requested that the end-user exemption be available to small financial entities (including credit unions, captive financial companies, registered dealers and registered portfolio managers) that fall below a threshold coherent with the size of the Canadian OTC derivatives market. Moreover, a commenter suggested allowing registered dealers to exercise the end-user exemption when hedging the risk of their affiliates, as long as such affiliates would qualify to exercise the end-user exemption on their own.	No change. See *Phase-in of the requirement to clear a mandatory clearable derivative* above. We note that the phase-in approach of the clearing requirement will allow the local provincial regulators to provide more clarity on the developing derivatives registration regime, and to use trade repository data to investigate whether thresholds or carve-outs are appropriate for certain types of entities, such as credit unions.
	A commenter stated that former paragraph 7(2)(c) should refer to an affiliated entity that is not subject to a registration requirement, or that is exempted from a registration requirement, under the securities legislation of a jurisdiction of Canada. Failing to include all exempt entities on a general basis may prevent access to the exemption even where there the policy rationale underlying the Draft Model Rule does not support it.	Change made. See revised paragraph 9(2)(c).
	A commenter proposed to add “at least” prior to “one of the counterparties is not a financial entity” to make it clear that the end-user exemption is also	Changes made. See revised paragraph 9(2)(a).

	available to two parties if neither of them is a financial entity.	
Former S. 8 – Intragroup exemption	Two commenters questioned the necessity of Form F1 in the context of securities regulation. A commenter suggested that the intragroup exemption be simplified such that transactions between 100% owned affiliates are exempt as long as certain conditions are met without the need for additional agreements or forms. Three commenters proposed that a Form F1 should be effective until withdrawn, unless updates or notifications of change to the originally filed form are submitted. Two other commenters requested that parties should be permitted to provide a listing of all types of transactions in a particular sub-asset class expected between them.	Change made. We note that the Committee believes that Form F1 is necessary in all cases, even for 100% owned affiliates. We note, however, that the annual filing requirement has been removed and replaced with a requirement to amend the original filing with a notification of material change.
	A commenter asked whether "prudentially supervised" is intended to refer to federally-regulated financial entities that are under the regulatory jurisdiction of the Office of the Superintendent of Financial Institutions.	No change. We note that "entities prudentially supervised on a consolidated basis" refers to two counterparties that are supervised on a consolidated basis either by the Office of the Superintendent of Financial Institutions (Canada), a government department or a regulatory authority of Canada or a jurisdiction of Canada responsible for regulating deposit-taking institutions.
	Two commenters suggested that the requirement that the entities prepare statements on a consolidated basis is not necessary and may unduly exclude affiliated entities that should otherwise properly be	No change. We note that the former paragraph 8(1)(b) is sufficiently broad to allow entities which do not prepare financial statements on a consolidated basis to rely on the Intragroup exemption.

	able to rely on the exemption. They suggested the adoption of the securities laws' "affiliate" definition.	
	A commenter suggested that transactions between credit unions and their centrals should benefit from the intragroup exemption.	No change. We note that the proposed phase-in of the clearing requirement provides temporary relief for credit unions and their centrals. The proposed phase-in of the clearing requirement will also allow the local provincial regulators to use trade repository data to investigate whether thresholds or carve-outs are appropriate for certain types of entities.
	A commenter pointed out that the documentation related to the intragroup exemption should be flexible and should refer to the CFTC and EMIR rules on the matter.	No change. We note that the Committee has reviewed the CFTC and EMIR rules on the matter and believes the Clearing Rule provides sufficient flexibility.
	A commenter suggested that it should be clarified that reference to "securities legislation of a jurisdiction of Canada" includes commodity futures and derivatives legislation.	No change. We note that "securities legislation" is defined in NI 14-101 and includes in Québec the *Derivatives Act*. In other jurisdictions, the relevant *Securities Act* applies. We further note that it is the intention of the Committee to respect the Scope Rules in the determinations to be made.
	A commenter would like confirmation that the intragroup exemption is available to registered dealers as long as they satisfy the necessary criteria.	No change. We note that the intragroup exemption applies to registered dealers as long as the criteria provided by the exemption are met.
	A commenter proposed that former paragraph 8(2)(c) could be shortened to simply stipulate the requirement for a written agreement setting out the terms of the transaction between the counterparties.	Changes made. See revised paragraph 10(2)(c).

Former S. 9 – Improper use of exemption	Three commenters requested clarification on how the local provincial regulators would determine that an entity has improperly used an exemption, and on the process by which the local provincial regulators would direct a local counterparty to submit a transaction for clearing under section 4.	Changes made. Former section 9 on Improper use of exemption has been removed as local regulators have the legal powers to enforce regulations.
Former S. 9 – Record keeping	A commenter pointed out that a party to an OTC derivatives transaction should be able to rely on representations made by the other party, without any further investigation or documentation, in order to determine whether the clearing requirement applies.	Changes made. See additional guidance included in Section 11 of the Clearing CP. We note, however, that certain conditions must be met for a local counterparty to rely on factual representations by the other counterparty.
	A commenter pointed out that, with respect to the requirement in former subsection 9(1) and specifically with respect to the Intragroup exemption, it should be sufficient that the records are kept by one of the “intragroup” parties.	No change. We note that it is not expected that documents or legal opinions be kept by each counterparty; however, both counterparties must be able to make copies of these agreements available to the regulator upon request.
	Three commenters questioned the necessity to obtain board approval for qualifying for the end-user exemption. A commenter suggested that a board of directors should be required to authorize the use of the end-user exemption no more than annually and requested that the CSA permit lower-tier entities to rely upon authorization from the board of directors of a higher-tier affiliate to exercise the exemption.	Changes made. See revised paragraph 11(1). End-users will not be required to obtain board approval in order to qualify for the end-user exemption.
	A number of commenters requested additional guidance and questioned the level of detail required as supporting	No change. We note that hedge-accounting compliant record-keeping is not a requirement for all hedging derivatives under the

	documentation with respect to each transaction for which the end-user exemption will be relied upon. They also expressed the opinion that it imposed a heavy regulatory burden on participants using this exemption. Notably, a number of commenters requested guidance on how the Committee requires entities to assess or document their hedging effectiveness.	Clearing Rule. However, hedges meeting the stricter accounting standards should be sufficient to meet the conditions of the end-user exemption.
Former S. 10–Non-Application	Two commenters requested that the non-application be extended to foreign governments, entities owned by foreign governments and recognized supra-national agencies, such as the International Monetary Fund.	Change made. See amendments made to section 6 on Non-Application. We note that non-application has not been extended to recognized supra-national agencies. The Committee expects to receive exemption requests from these entities.
	A commenter requested that the non-application should be extended to entities wholly owned by a federal, or provincial government, **or** to entities whose obligations are guaranteed by a federal or provincial government. Another commenter proposed that the non-application should be extended when a crown corporation or other corporation owned by the government is an agent of the Crown without a guarantee being in place. Another commenter argued that government-related entities that are also agents of the Crown should be granted the same immunity through former section 10 as government.	No change. We note that in the case of entities wholly owned by the government of Canada, a government of a jurisdiction of Canada or a government of a foreign jurisdiction, the non-application is only extended to those entities whose obligations are guaranteed, respectively, by the government of Canada, a government of a jurisdiction of Canada or a government of a foreign jurisdiction.
	A number of commenters were opposed to the non-application of the Draft Model Rule to federal and provincial governments and to government entities. A	No change. We note that the local provincial regulators retain the right to modify the applicability of all exemptions and may register certain entities given the

	commenter suggested limiting the application of former section 10 only to those government entities whose OTC derivatives portfolios are not in excess of a certain threshold.	size of their activities.
Former S. 12 – Transition	Two commenters suggested that parties should not have to clear transactions entered into before the coming into force of this rule if they are "materially amended" as this requirement may deter parties from making amendments for legitimate purposes. Two commenters requested confirmation that the end-user and intragroup exemptions will apply to Material Changes.	No change. See the interpretation of material amendment in the Clearing CP. We note that the end-user and intragroup exemptions will apply to material amendments.
	A commenter suggested that an objective test would be beneficial to determine whether an amendment is material.	No change. We note that the Committee considers that the proposed approach provides flexibility as an entity should be able to establish whether a transaction was amended materially. Guidance on material amendments is provided in the Clearing CP.
Form F1	A commenter requested that the word "application" be removed from section 3 of the form. A commenter asked whether this information will be accessible to the public.	Changes made. We note that Form F1 is a notice filing and not an application.
Form F2	A commenter requested that the access given to regulators be limited to "applicable" books and records.	Changes made. See revised Form F2.

List of Commenters

1. Atlantic Central
2. Bruce Power L.P.
3. Caisse de dépôt et placement du Québec
4. Canadian Bankers Association
5. Canadian Commercial Energy Working Group submitted by Sutherland Asbill & Brennan LLP
6. CanadianLife and Health Insurance Association Inc.
7. Capital Power
8. Central 1
9. Canadian Market Infrastructure Committee
10. Concentra Financial
11. Enbridge Inc.
12. Encana Corporation
13. Énergie NB Power
14. Financial Institutions Commission
15. Ford Motor Company
16. FortisBC Energy Inc.
17. Global Foreign Exchange Division
18. IGM Financial Inc.
19. International Swaps and Derivatives Association
20. Investment Industry Association of Canada
21. Just Energy Group Inc.
22. KfW Bankengruppe
23. LCH.ClearnetGroup Limited
24. New Brunswick Investment Management Corporation
25. Pension Investment Association of Canada
26. Sask Energy Incorporated
27. Sask Power
28. Shell Trading
29. Stewart McKelvey
30. Suncor Energy Inc.
31. TMX Group Limited
32. Trans Canada Corporation
33. Tri Optima AB
34. Western Union Business Solutions