CSA/ACVM Canadian Securities Administrators Autorités canadiennes en valeurs mobilières

CSA Notice and Second Request for Comment Proposed Amendments to National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives* and Proposed Changes to Companion Policy 94-101 *Mandatory Central Counterparty Clearing of Derivatives*

September 3, 2020

Introduction

The Canadian Securities Administrators (the **CSA** or we) are publishing the following for a second comment period of 90 days, expiring on December 2, 2020:

- proposed amendments to National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives* (the **National Instrument)**, and

- proposed changes to Companion Policy 94-101 *Mandatory Central Counterparty Clearing of Derivatives* (the **CP**).

Collectively, the proposed amendments to the National Instrument (the **Proposed Rule Amendments**) and the proposed changes to the CP are referred to as the **Proposed Amendments**.

The CSA is of the view that Proposed Rule Amendments are necessary to address issues raised by market participants following the CSA's publication for comment of proposed amendments and changes to the National Instrument and the CP on October 12, 2017 (the **2017 Proposed Amendments**). The issues relate largely to the scope of market participants that are required to clear an over-the-counter (**OTC**) derivative prescribed in Appendix A to the National Instrument through a central clearing counterparty (the **Clearing Requirement**).

We are issuing this CSA Notice to solicit comments on the Proposed Amendments.

Background

The Proposed Amendments are a response to feedback received from various market participants, and are intended to more effectively and efficiently promote the underlying policy aims of the National Instrument.

The National Instrument was published on January 19, 2017 and came into force on April 4, 2017 (except in Saskatchewan where it came into force on April 5, 2017). The purpose of the National Instrument is to reduce counterparty risk in the OTC derivatives market by

requiring certain counterparties to clear certain prescribed derivatives through a central clearing counterparty.

The Clearing Requirement became effective for certain counterparties specified in paragraph 3(1)(a) of the National Instrument (*i.e.*, a local counterparty that is a participant of a regulated clearing agency that subscribes for clearing services for the applicable class of derivatives) on the coming-into-force date of the National Instrument, and was initially scheduled to become effective for certain other counterparties specified in paragraphs 3(1)(b) and 3(1)(c) on October 4, 2017.

On October 12, 2017 the CSA published for comment proposed amendments and changes to the National Instrument and CP. However, in order to facilitate the rule-making process for these amendments and to refine the scope of market participants that are subject to the Clearing Requirement, the CSA jurisdictions (except Ontario) exempted counterparties specified in paragraphs 3(1)(b) and (c) of the National Instrument from the Clearing Requirement.[1]

The Ontario Securities Commission (the **OSC**) similarly amended the National Instrument to extend the effective date of the Clearing Requirement for those counterparties until August 20, 2018.[2]

While the Clearing Requirement took effect in Ontario on August 20, 2018 for all categories of counterparties specified in subsection 3(1) of the National Instrument, OSC staff expressed the view that only counterparties specified under paragraph 3(1)(a) are expected to comply with the Clearing Requirement until the CSA finalizes the amendments to the National Instrument to narrow the scope of market participants that would be subject to the Clearing Requirement[3].

Substance and Purpose of the Proposed Amendments

Following the comments received on the 2017 Proposed Amendments, the CSA is proposing further amendments to the National Instrument. These include amendments that reflect issues raised by commenters relating to the scope of the counterparties that are subject to the National Instrument, and amendments to refine the scope of products that are mandated to be cleared. Minor non-material changes are also being proposed.

The Proposed Amendments reflect our consideration of the comments received from market participants on the 2017 Proposed Amendments, as well as our ongoing review of

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[1] Blanket Order 94-501, available on the website of the securities regulatory authority in the local jurisdiction.

[2] See, in Ontario, Amendment to National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives*, published July 6, 2017.

[3] As explained further in CSA Staff Notice 94-303, on May 31st 2018 the CSA jurisdictions (except Ontario) extended the blanket order relief under Blanket Order 94-501 until the earlier of its revocation or the coming into force of amendments to the National Instrument with respect to the scope of counterparties subject to the Clearing Requirement. Since blanket orders were not authorized under Ontario securities law, the OSC was unable to follow the approach of the other CSA jurisdictions.

the National Instrument's impact on market participants.

Summary of the Proposed Amendments

(a) Subsection 1(2): interpretation of "affiliated entity"

The proposed amendments to the interpretation of "affiliated entity" are based on the concept of consolidated financial statements under IFRS or U.S. generally accepted accounting principles[4]. Proposed subsection 1(2), in conjunction with the proposed repeal of subsection 1(3) and the introduction of subsections 3(0.1) and (0.2), would affect the circumstances in which an entity is considered an affiliated entity.

The proposed amendments reflect a CSA policy decision in 2016, in response to our evaluation of the size and nature of the Canadian OTC derivatives market, to design the Clearing Requirement so that it applied to specific types of transactions and to the market participants that had access to clearing agencies that offered clearing services for the mandated derivatives, or because certain market participants' derivatives exposure represented a potential systemic risk. Considering the scope of the application of the National Instrument and review of the comments received following the publication of the 2017 Proposed Amendments, the previous interpretation of "affiliated entity" could subject certain entities to the Clearing Requirement unintentionally while other market participants could unintentionally be excluded from the National Instrument.

(b) De minimis exclusion

Consistent with the CSA's intention to apply the Clearing Requirement only to market participants that, together with affiliated entities, might present systemic risk, the CSA is still proposing to exclude from the scope of the National Instrument entities that have a month-end gross notional amount under all outstanding derivatives of less than $1 billion and are part of a large derivative participant group from the Clearing Requirement.

Paragraph 3(1)(c) was originally designed to capture certain large local counterparties and all their local affiliated entities. In substance, adding the notional amount of all outstanding derivatives of affiliated entities to the calculation of the threshold stated in paragraph 3(1)(c) was intended to prevent market participants from creating multiple sub-entities to avoid being subject to the Clearing Requirement. However, the CSA is of the view that entities with less than $1 billion of notional derivatives exposure should not be required to clear.

In response to comments we received following the publication of the 2017 Proposed Amendments to reduce the monitoring frequency of the $1 billion threshold under paragraphs 3(1)(b) and (c), the CSA is proposing to establish an annual three-month monitoring period during which counterparties will need to determine if they are subject to

[4] Refer to IFRS 10 Consolidated Financial Statements and US FASB Accounting Standards Codification Topic 810.

the Clearing Requirement for the subsequent one-year period.

(c) Investment funds and special purpose entities

The CSA has come to the view that a further subset of market participants should be excluded. With the introduction of subsections 3(0.1) and (0.2), it is proposed to exclude investment funds and certain types of consolidated entities (commonly referred to as special purpose entities) from being treated as affiliated entities for the purpose of paragraphs 3(1)(b) and (c), with the effect that such entities would only be potentially subject to the Clearing Requirement in circumstances where paragraph 3(1)(c) applies, i.e. when these entities exceed on their own the $500 billion threshold in that paragraph.

(d) Determination of mandatory clearable derivatives

As previously published in the 2017 Proposed Amendments, Appendix A of the National Instrument will remove overnight index swaps with variable notional type and forward rate agreements with variable notional type from the list of mandatory clearable derivatives as those are not currently offered for clearing by regulated clearing agencies.

(e) Appendix B Laws, Regulations or Instruments of foreign jurisdiction applicable for substituted compliance

The CSA continues to follow developments regarding Brexit and other international actions being taken in that regard to ensure the substituted compliance provision reflect any changes that are necessary to address these developments.

(f) Removal of the requirement to deliver Form 94-101F1 Intragroup Exemption and Form 94-101F2 Derivatives Clearing Services

The CSA is proposing to remove the requirement to deliver Form 94-101F1 *Intragroup Exemption* and Form 94-101F2 *Derivatives Clearing Services* from the National Instrument because we have found alternative sources for obtaining the information included in these forms that does not result in additional regulatory burden for participants.

Contents of Annexes

The following annexes form part of this CSA Notice:

Annex A Proposed amendments to National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives*

Annex B Blackline of National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives* showing the proposed amendments

Annex C Proposed Changes to Companion Policy 94-101 *Mandatory Central Counterparty Clearing of Derivatives*

Annex D Blackline of Companion Policy 94-101 *Mandatory Central Counterparty Clearing of Derivatives* showing the proposed changes

Annex E Summary of comments and CSA responses and list of commenters

Annex F Local Matters, where applicable

Request for Comments

Please provide your comments in writing by December 2, 2020. We cannot keep submissions confidential because securities legislation in certain provinces requires publication of a summary of the written comments received during the comment period.

In addition, all comments received will be posted on the websites of the Alberta Securities Commission (www.albertasecurities.com), the Autorité des marchés financiers (www.lautorite.qc.ca) and the Ontario Securities Commission (www.osc.gov.on.ca).

Therefore, you should not include personal information directly in comments to be published.

It is important that you state on whose behalf you are making the submission.

Thank you in advance for your comments.

Please address your comments to each of the following:

British Columbia Securities Commission;

Alberta Securities Commission;

Financial and Consumer Affairs Authority of Saskatchewan;

Manitoba Securities Commission;

Ontario Securities Commission;

Autorité des marchés financiers ;

Financial and Consumer Services Commission (New Brunswick);

Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island;

Nova Scotia Securities Commission;

Office of the Superintendent of Securities, Newfoundland and Labrador;

Office of the Superintendent of Securities, Northwest Territories;

Office of the Yukon Superintendent of Securities; and

Nunavut Securities Office;

Please send your comments only to the following addresses. Your comments will be forwarded to the remaining jurisdictions:

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Questions

If you have questions about this CSA Notice, please contact any of the following:

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