

Can Canada effectively regulate Derivatives Central Counterparties?

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“There is no use carrying an umbrella if your shoes are leaking”
Irish Proverb

Abstract

Derivatives Central Counterparties (CCPs) have made it to the forefront of the current financial market regulatory reform as a major solution to mitigate systemic risk and address the weaknesses in the market infrastructure of the global over-the-counter (OTC) derivatives markets that were exposed during the crisis. This is the underlying rationale for the current G-20 regulatory drive to move all standardised derivatives towards centralized clearing by end 2012. To implement this G-20 clearing mandate, some countries have adopted or plan to adopt a systemic functional approach to the regulation of CCPs as part of a macro-prudential regulation under the broad remit of financial stability. Legislative proposals, discussion and consultation papers and/or drafted legislation are geared towards creating an effective regulatory and oversight framework for CCPs that would be commensurate to the risks they are intended to address. This systemic approach to CCP regulation is underpinned by the vital role of CCPs in the financial system as a whole and the impact of their operations to financial stability.

According to the Financial Stability Board’s (FSB) recent implementation progress report of April 2011, Canada has not gone as far in its implementation of the G-20 clearing mandate. Though published reports by Canadian financial and market regulators indicate a cognizance of the systemic importance of CCPs and the need for their effective regulation and oversight, there has been a puzzling lack of public discourse so far on what approach such regulation would take. The only indication of the direction of a possible regulatory approach governing CCPs comes from a vague statement made by the Canadian Securities Administrators (CSA), that they would be primarily regulated by securities regulators in their province of operations.¹

This paper will mainly examine if such a Canadian regulatory framework for CCPs would fit the tenets and principles of effective regulation bearing in mind the role of CCPs in the Canadian financial system.

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¹ See CSA Consultation Paper 91-401 on Over-the-Counter Derivatives Regulation in Canada, published in November 2010 at page 24. In contrast, see Bank of Canada’s Carol Ann Northcott’s presentation “*Central Counterparties and Systemic Risk*” to the Canadian Derivatives Conference on 14 October 2010