



**CANADIAN SECURITIES
ADMINISTRATORS PUBLISH
MODEL PROVINCIAL RULES –
*DERIVATIVES: PRODUCT
DETERMINATION AND
TRADE REPOSITORIES AND
DERIVATIVES DATA
REPORTING***

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Canadian Securities Administrators Publish Model Provincial Rules – *Derivatives: Product Determination and Trade Repositories and Derivatives Data Reporting*

I. INTRODUCTION

On December 6, 2012, the Canadian Securities Administrators OTC Derivatives Committee (the “**Committee**”) published model provincial rules for a sixty (60) day comment period. The model rules include:

- Model Provincial Rules – *Derivatives: Product Determination* (the “**Scope Rule**”) and the Model Explanatory Guidance to Model Provincial Rule – *Derivatives Product Determination*; and
- Model Provincial Rule – *Trade Repositories and Derivatives Data Reporting* (the “**TR Rule**”) and the Model Explanatory Guidance to Model Provincial Rule – *Trade Repositories and Derivatives Data Reporting*.

Collectively, the Committee has referred to all of the above as the “Model Rules.”

In collaboration with the Canadian over-the-counter (“**OTC**”) Working Group,¹ the Committee has published a series of derivatives consultation papers since November 2010² outlining policy recommendations for the regulation of OTC derivatives in Canada. The regulatory framework developed by the Canadian OTC Working Group will be implemented through provincial rules. The Model Rules have been drafted using the model of the Ontario Securities Act. The Committee indicates that subsequent model rules will be drafted based on other provincial statutes.

*Please note, the below is a high-level summary only. Fraser Milner Casgrain LLP (“**FMC**”) will be publishing a more in-depth commentary in the future which includes a comparison of the relevant and applicable U.S. Commodity Futures Trading Committee’s (“**CFTC**”) final rules.*

II. THE SCOPE RULE

The Committee indicates that:

¹ The Canadian OTC Derivatives Working Group consists of the Bank of Canada, the Federal Department of Finance, the Office of the Superintendent of Financial Institutions, the Alberta Securities Commission, the Autorité des marchés financiers, the British Columbia Securities Commission and the Ontario Securities Commission.

² Previously published consultation papers include: [Canadian Securities Administrators Consultation Paper 91-401 on Over-the-Counter Derivatives Regulation in Canada](#); [Canadian Securities Administrators Consultation Paper 91-402 on Derivatives: Trade Repositories](#); [Canadian Securities Administrators Consultation Paper 91-403 on Derivatives: Surveillance and Enforcement](#); [Canadian Securities Administrators Consultation Paper 91-404 on Derivatives: Segregation and Portability in OTC Derivatives Clearing](#); [Canadian Securities Consultation Paper 91-405 on Derivatives: End-User Exemption](#) and [Canadian Securities Administrators Consultation Paper 91-406 – Derivatives: OTC Central Counterparty Clearing](#).

[t]he Scope Rule provides a foundation for the regulation of derivatives that is both responsive and flexible. The broad definition of “derivative” in existing and proposed provincial securities legislation is intended to include the types of instruments traditionally referred to as derivatives (for example, swaps and forwards) as well as other novel instruments. Legislation in many Canadian jurisdictions contemplates that an instrument that meets the general definition of derivative may be treated as a derivative, a security, or be excluded in whole or in part from regulation.

The Committee drafted the Scope Rule to resolve conflicts that arise when a contract or instrument meets both the definition of “derivative”³ and “security”⁴ under applicable provincial legislation. The Scope Rule purports to classify which contracts or instruments are to be regulated as derivatives, securities or outside the scope of both derivatives and securities legislation altogether.

The Scope Rule prescribes that the following contracts and instruments will not be considered to be “derivatives” and subject to derivatives regulation, as follows:

- regulated by gaming control legislation of Canada or a province;
- an insurance or annuity contract issued by an insurer holding a license under insurance legislation or Canada or a province;
- a spot market contract or instrument for the purchase and sale of currency:
 - that requires the counterparties to make or take physical delivery of the currency within two business days and does not allow for the contract or instrument to be rolled over;
 - that does not allow for cash settlement in place of physical delivery of the foreign currency; and
 - that is intended by the counterparties to be physically settled;
- **a contract or instrument for immediate or deferred delivery of a physical commodity other than cash or a currency:**
 - **that requires the counterparties to make or take physical delivery;**
 - **that does not allow for cash settlement in place of physical delivery; and**
 - **that is intended by the counterparties to be physically settled;**
- a contract or instrument that is a derivative under subsection X [Definitions] of the Act (i.e. this definition is still to be determined/proclaimed by the Committee) and is evidence of a deposit issued by a bank listed in Schedule I, II or III to the Bank Act

³ A definition of derivative is not provided in the Model Rules.

⁴ A definition of security is not provided in the Model Rules; one should look to the relevant securities legislation of their respective securities regulator.

(Canada), by an association to which the Cooperative Credit Associations Act (Canada) applies or by a company to which the Trust and Loan Companies Act (Canada) applies; or

- a contract or instrument that is a derivative under subsection X [Definitions] of the Act and is evidence of a deposit issued by a credit union or league to which the *Credit Unions and Caisses Populaires Act, 1994* or a similar statute of a province (other than Ontario) or territory of Canada applies or by a loan corporation or trust corporation registered under the Loan and Trust Corporations Act or a similar statute of a province (other than Ontario) or territory of Canada.

With respect to the bolded bullet point above regarding contracts or instruments for immediate or deferred delivery of a physical commodity other than cash or a currency, this exemption is relevant to those Canadian entities that enter into OTC energy derivative transactions and is similar to the CFTC's forward contract exclusion.

All contracts or instruments (that are not captured in the listing above) that are securities and otherwise derivatives are prescribed not to be derivatives; derivatives that are securities. As well, the Committee indicates that all contracts or instruments that would otherwise be derivatives (that are not captured in the listing above), are prescribed not to be derivatives if such contract or instrument is used by an issuer or an affiliate of an issuer solely to compensate an employee or service provider or as a financing instrument and whose underlying interest is a share or stock of that issuer or its affiliate; derivatives prescribed to be securities.

The Scope Rule will only apply for the purposes of the TR Rule. Until the Scope Rule has been extended to other derivatives rule-making areas, any legislation, rules, notices or other policies applicable to derivatives will continue to apply. For example, Ontario Securities Commission Staff Notice 91-702 – *Offerings of Contracts for Difference and Foreign Exchange Contracts to Investors in Ontario* (or in the instance of Alberta, the Alberta Securities Commission Blanket Order 91-503 – *Over-the-Counter Derivatives Transactions and Commodity Contracts* or its replacement or in the instance of New Brunswick, the New Brunswick Securities Commission Local Rule 91-501 - *Derivatives*).

I. THE TR RULE

The Commission indicates that:

[t]he purpose of the TR Rule is to improve transparency in the derivatives market to regulators and the public, and ensure that designated trade repositories operate in a manner that promotes the public interest. Trade repository data is essential for regulatory oversight of the derivatives market. This oversight will allow regulators to address a variety of risks including monitoring of systemic risk and the risk of market abuse. Derivatives data reported to designated trade repositories will also assist policy-making by providing regulators with information on the nature and characteristics of the Canadian derivatives market.

Generally, the TR Rule describes requirements for the operation and ongoing regulation of designated or recognized trade repositories⁵ (a “**trade repository**”), and the mandatory reporting of derivatives transaction data by market participants.

The TR Rule is broken down into the following primary topics:

- Trade Repository Designation and Ongoing Requirements
- Data Reporting
- Data Dissemination and Access to Data
- Exemptions to the TR Rule

A. Trade Repository Designation and Ongoing Requirements

The TR Rule contains rules for trade repository designation and ongoing requirements for trade repositories.

Generally, in order to obtain and maintain a designation as a trade repository, a person or entity must comply with the TR Rules in addition to all of the terms and conditions which may be set out in any recognition order made by the [applicable local (i.e. provincial or territorial) securities regulator.

The Commission states that:

While there is no prohibition on an undesignated trade repository operating in [Province x], a market participant using it would not be in compliance with reporting obligations.

B. Data Reporting

The TR Rule outlines reporting obligations of counterparties of transactions and includes a description of the counterparties that will be subject to the duty to report, requirements as to the timing of reports and a description of the data that is required to be reported.

Duty to Report, Real-time Reporting

This part of the TR Rule prescribes that a local counterparty⁶ must report (or cause to be reported) to a designated trade repository relevant derivatives data for each transaction to

⁵ Ontario is the only Canadian jurisdiction which has defined the term “trade repository” to date; “**trade repository**” means a person or company that collects and maintains reports of completed trades by other persons and companies, and a “**designated trade repository**” means a trade repository that is designated by the Commission.

⁶ “**local counterparty**” means a party to a transaction if, at the time of the transaction, any of the following applies: (a) the party is an individual who is a resident of [Province x]; (b) the party is a person or company, other than an individual, organized under the laws of [Province x] or that has its head office or principal place of business in [Province x]; (c) the party is a reporting issuer under the securities legislation of [Province x]; (d) the party is a registrant under the securities legislation of

which it is a counterparty. This reporting must be done by the reporting counterparty (i.e. the party required to report derivatives data to a trade repository) as soon as technologically possible. If it is not technologically practicable to report in real time, the reporting counterparty must make the report as soon as technologically practicable and in no event later than the end of the next business day following the day of the entering into of the transaction, change or event that is to be reported.

The reporting counterparty must ensure that all reported derivatives data relating to a particular transaction:

1. is reported to the same designated trade repository or **[applicable local securities regulator]** to which the initial report was made; and
2. is accurate and contains no misrepresentations.

Determining the Reporting Counterparty

Generally, the counterparty required to report derivatives data for a transaction is determined as follows:

1. if the transaction is between a “derivatives dealer”⁷ and a counterparty that is not a derivatives dealer, the derivatives dealer is the reporting counterparty; and
2. in any other case, both counterparties are reporting counterparties unless they agree in writing between themselves that one of them is to be the reporting counterparty.

Pre-existing Derivatives

Generally, a local counterparty to a transaction entered into before the day Model Rule comes into force, that had outstanding contractual obligations on that day, must report (or cause to be reported) the derivatives data in relation to that transaction to a designated trade no later than three hundred and sixty-five (365) days after the Model Rule is in effect.

Records of Data Reported

Local counterparties to a transaction must keep records of the derivatives data in relation to the derivative for the life of the derivative and for a further seven (7) years after the date on which

[Province x]; (e) the party negotiates, executes, settles, writes or clears any part of the transaction in **[Province x]**; or (f) the party is a subsidiary of a person or company, or group of persons and companies, described in any of paragraphs (a) to (d).

⁷ The term “derivatives dealer” is not defined in the Model Rules, nor is it defined in local (i.e. provincial or territorial) securities legislation. The Committee indicates in the Model Explanatory Guidance to Model Provincial Rule – *Trade Repositories and Derivatives Data Reporting*, that the terms “derivative” “dealer” are both defined in the *Securities Act* (Ontario) and the term “derivatives dealer” takes its meaning from the combination of these definitions.

the derivative expires or terminates; records must be kept in a safe location and in durable form.

The TR Rule also discusses requirements related to legal identifier requirements, transaction identifiers, product identifiers, creation data, life-cycle data and valuation data. These requirements will be discussed further in a FMC in-depth commentary in the future which includes a comparison of the relevant and applicable CFTC final rules.

C. Data Dissemination and Access to Data

The TR Rule requires all designated trade repositories conform to internationally accepted regulatory access standards and to provide electronic access to applicable local securities regulators to data required or requested by the regulatory. Further, the TR Rule requires designated trade repositories to provide relevant transaction data to counterparties and to have appropriate verification and authorization in place to deal with access to data information by non-reporting counterparties.

Finally, the TR Rule requires designated trade repositories to, on a periodic basis, create and make available to the public, aggregate data on transactions reported to it as well as transaction level reports of the principal economic terms of each transaction reported to it not later than:

1. one (1) day after receiving those terms from the reporting counterparty to the transaction, if one of the counterparties to the transaction is a derivatives dealer; and
2. two (2) days after receiving those terms from the reporting counterparty to the transaction in all other circumstances.

A designated trade repository must disseminate and provide access to the above noted data at its own cost.

D. Exemptions to the TR Rule

The TR Rule contains a general exemption to the TR Rule as may be granted by the “Director” (which term is not defined), subject to any conditions or restrictions which may be imposed. The TR Rule also prescribes that there is no obligation under this Rule for a local counterparty to report derivatives data in relation to a physical commodity transaction if the local counterparty:

1. is not a dealer or adviser; and
2. has less than \$500,000 aggregate notional value, (without netting), under all its outstanding transactions, at the time of the transaction including the additional notional value related to that transaction.

II. EFFECTIVE DATE

The Model Rules prescribe no effective date for Canada (i.e. all provinces and territories). However, the Model Rules do suggest that in Ontario, portions of the Model Rule dealing with

definitions, trade repository designation and ongoing requirements, data dissemination and exemptions shall become effective fifteen (15) days of the TR Rule is approved by the Minister.⁸

Generally, the portion of the TR Rule which prescribes data reporting requirements shall become effective six (6) months after the date the initial portions of the TR Rule are effective.

III. NOTES

We invite market participants and other stakeholders to discuss any comments and questions with us. If you require any assistance in commenting on the Model Rules we are available to assist you. **Comments on the Model Rules may be submitted to the Canadian Securities Administrators prior to February 4, 2013.**

For more information regarding the Commission's derivatives regulation initiatives and the proposed Canadian OTC derivative regulatory regime being established by the Commission and the Canadian OTC Working Group and how it could impact your derivatives and commodity trading operations, please contact:

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This summary provides only an outline and does not constitute legal advice. Specific legal advice should be obtained before making any decisions regarding the Model Rules.

⁸ Under the Ontario Securities Act, "Minister" means the Minister of Finance or such other member of the Executive Council to whom the administration of this Act may be assigned.