

## CSA Notice and Request for Comment

***Proposed National Instrument 94-102 Derivatives: Customer Clearing and Protection of Customer Collateral and Positions***

***Proposed Companion Policy 94-102CP Derivatives: Customer Clearing and Protection of Customer Collateral and Positions***

**January 21, 2016**

### **I. Introduction**

We, the Canadian Securities Administrators (the **CSA**) are publishing the following for a ninety (90) day comment period, expiring on April 19, 2016:

- Proposed National Instrument 94-102 *Derivatives: Customer Clearing and Protection of Customer Positions and Collateral* (the **Instrument**);
- Proposed Companion Policy 94-102CP *Derivatives: Customer Clearing and Protection of Customer Positions and Collateral* (the **CP**).

Collectively, the Instrument and the CP will be referred to as the **Proposed National Instrument**.

We are issuing this notice to provide interim guidance and solicit comments on the Proposed National Instrument.

We would also like to draw your attention to the recent publication of National Instrument 24-102 *Clearing Agency Requirements* and the upcoming publication of Proposed National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives* and in particular the scope of application of mandatory clearing requirements. These publications, including the Proposed National Instrument, relate to central counterparty clearing. We therefore encourage the public to consider these publications comprehensively.

### **II. Background**

On January 16, 2014, the CSA OTC Derivatives Committee (the **Committee**) published CSA Notice 91-304 *Proposed Model Provincial Rule on Derivatives: Customer Clearing and Protection of Customer Positions and Collateral* (the **Model Rule**). The Committee invited public comments on all aspects of the Model Rule. Twenty-two comment letters were received. A list of those who submitted comments, as well as a chart summarizing the comments received and the Committee's responses are attached in Annex A to this

Notice. Copies of the comment letters can be found on the CSA members' websites.<sup>1</sup>

The Committee has carefully reviewed the comments received and has made determinations on appropriate revisions to the Model Rule, which has been transformed into the Proposed National Instrument for the purpose of adopting a harmonized instrument across Canada.

Following the expiry of the comment period, the Committee will review all comment letters received in respect of the Proposed National Instrument to make recommendations on changes at a Committee level.

### **III. Substance and Purpose of the Proposed National Instrument**

Canadian and international initiatives promoting the clearing of over-the-counter (**OTC**) derivative transactions will cause certain market participants, who are not clearing members at a derivatives clearing agency, to clear their OTC derivatives transactions indirectly through market participants that are clearing members or otherwise provide clearing services. The purpose of the Instrument is to ensure that customer clearing is carried out in a manner that protects customer collateral and positions and improves derivatives clearing agencies' resilience to a clearing member default. For a more detailed explanation of customer clearing please see CSA Consultation Paper 91-404 *Derivatives: Segregation and Portability in OTC Derivatives Clearing*.<sup>2</sup>

The Instrument contains requirements for the treatment of customer collateral by clearing intermediaries and derivatives clearing agencies, including requirements relating to the segregation and use of customer collateral. These requirements are intended to ensure that customer collateral is protected, particularly in the case of financial difficulties of a clearing intermediary. The Instrument includes detailed record-keeping, reporting and disclosure requirements intended to ensure that customer collateral and positions are readily identifiable. The Instrument also contains requirements relating to the transfer or porting of customer collateral and positions intended to ensure that, in the event of default or insolvency of a clearing intermediary, customer collateral and positions can be transferred to one or more non-defaulting clearing intermediaries without having to liquidate and re-establish the positions.

### **IV. Summary of the Instrument**

Part 1 of the Instrument sets out relevant definitions, and specifies that the Instrument applies only to trades in derivatives where a customer, regulated clearing agency member or clearing intermediary has a specified nexus to a local jurisdiction.

Part 2 to Part 4 of the Instrument set out requirements applicable to clearing intermediaries with respect to treatment of customer collateral, record keeping and disclosure.

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<sup>1</sup> Available at <http://www.osc.gov.on.ca/en/43833.htm>.

<sup>2</sup> Available at [www.osc.gov.on.ca](http://www.osc.gov.on.ca).

Part 2 of the Instrument sets out the manner in which customer margin and collateral is to be treated by clearing intermediaries. This Part sets out requirements in respect of the collection, holding and maintenance of customer collateral, the identification of excess margin as well as the segregation, use and investment of customer collateral. Part 2 also sets out requirements for a clearing intermediary to be able to provide clearing services to a customer, and for appropriate risk management in respect of those services.

Under Part 3 of the Instrument, clearing intermediaries are required to keep and retain certain records and supporting documentation, and keep adequate and appropriately updated books and records that will facilitate the identification and protection of customer positions and collateral.

Part 4 of the Instrument sets out disclosure requirements for clearing intermediaries as well as reports required to be submitted to the regulator or the securities regulatory authority.

Part 5 to Part 7 of the Instrument are parallel to Part 2 to Part 4 of the Instrument, and set out similar requirements as they apply to regulated clearing agencies.

Part 5 of the Instrument sets out how customer margin and collateral is to be treated by regulated clearing agencies. This Part sets out requirements in respect of the collection, holding and maintenance of customer collateral, the identification of excess margin as well as the segregation, use and investment of customer collateral.

Under Part 6 of the Instrument, regulated clearing agencies are required to keep certain records and supporting documentation as well as keep adequate and appropriately updated books and records that will facilitate the identification and protection of customer positions and collateral.

Part 7 of the Instrument sets out disclosure requirements for regulated clearing agencies as well as reports required to be submitted to the regulator or the securities regulatory authority.

Part 8 of the Instrument sets out the requirements for a regulated clearing agency to facilitate the transfer of customer positions and collateral in the context of a clearing intermediary's default, or at the request of a customer, under certain specified conditions. Part 8 also requires a clearing intermediary to have policies and procedures for transferring of customer positions and collateral, when the clearing intermediary provides clearing services to an indirect intermediary.

Under Part 9 of the Instrument, clearing intermediaries and regulated clearing agencies located in foreign jurisdictions may be exempted from compliance with the Instrument where they meet certain requirements set out in the Instrument, including by complying with similar legislation in their home jurisdiction.

Part 10 of the Instrument contains provisions authorizing the regulator or the securities regulatory authority, as the case may be, to grant an exemption from any provision of the Instrument.

Part 11 of the Instrument sets out relevant effective dates for the Instrument.

## **V. Changes Reflected in the Proposed National Instrument**

### ***(a) Fundamental Changes to Model Rule***

#### **Acceptable Clearing Models**

There are various customer clearing models available in the global OTC derivatives market.<sup>3</sup> The Committee believes that it is important for local customers to have the option to use the model or models that are most suitable for their needs, provided that each model available provides adequate protection for customer positions and collateral. A fundamental comment received during the consultation process was that the Model Rule did not facilitate the operation of certain widely used customer clearing models.<sup>4</sup> In response, the Committee has made significant revisions to the Instrument that make a broader range of clearing models available to local customers. This revised approach has led to revisions throughout the Instrument.

Due to the variety of customer clearing models and legal frameworks supporting these models, the Instrument, as revised, potentially permits a wider range of clearing agencies to offer their customer clearing models in Canada. To enhance customer protection, the approval and oversight process for recognized or exempt clearing agencies will involve a thorough review of the customer safeguards provided by each clearing agency offering customer clearing in a jurisdiction of Canada.

#### **Scope of Application of the Instrument**

The Model Rule was drafted in a broad manner to apply where any participant in the customer clearing chain (i.e., the customer, a clearing intermediary and/or the clearing agency) was located in a jurisdiction of Canada. Comments were received that this application was overly broad. The Instrument has been revised to apply to a clearing intermediary or foreign clearing agency only where it is involved in a transaction with a local customer. The requirements applicable to regulated clearing agencies apply to any regulated clearing agency located in a jurisdiction of Canada for transactions with both local and foreign customers.

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<sup>3</sup> For example, the futures commission merchant model is available in the U.S. and the principal-to-principal model is available in the EU.

<sup>4</sup> In particular the comments received indicated that the Model Rule was not compatible with the principal-to-principal model.

***(b) Other changes to the Model Rule***

***(i) Clearing Intermediaries***

The Model Rule was designed such that only one clearing intermediary was permitted to be involved in a customer cleared transaction. The Committee acknowledges that this approach is not consistent with international market structures. Therefore, the Instrument has been revised to permit the involvement of multiple clearing intermediaries in a transaction. Each clearing intermediary involved in a transaction is therefore subject to the full requirements of the Instrument in order to ensure that no significant additional risk is introduced to the customer clearing chain.

***(ii) Substituted Compliance***

Currently, OTC derivative clearing infrastructure and service providers are largely concentrated outside of Canada. Therefore, it is likely that many local customers' cleared transactions will involve foreign infrastructure or market participants. As a result, the Committee has carefully considered the interaction of the Instrument with other foreign customer clearing regimes that may also impact a transaction involving local market participants or infrastructures. The Committee is proposing substituted compliance in specified circumstances where a foreign entity is involved in a transaction and appropriate foreign laws apply.

***(c) Miscellaneous drafting clarifications***

There are a number of non-substantive drafting changes, including a re-ordering of the Parts to separate requirements applicable to clearing intermediaries from those applicable to regulated clearing agencies.

**VI. Application of local rules for Derivatives: Product Determination**

The Committee intends that Ontario Securities Commission Rule 91-506 *Derivatives: Product Determination*,<sup>5</sup> Manitoba Securities Commission Rule 91-506 *Derivatives: Product Determination*,<sup>6</sup> Québec Regulation 91-506 *respecting Derivatives Determination*<sup>7</sup> and the Multilateral Instrument 91-101 *Derivatives: Product Determination*<sup>8</sup> (collectively, the **Product Determination Rules**) will be applicable to the Instrument. Therefore, in all local jurisdictions, transactions that are cleared on behalf of a customer that fall within the scope of the applicable Product Determination Rules would be subject to the Instrument. We note that once the Proposed National Instrument is in force, Regulation 91-506 respecting Derivatives Determination will be amended to

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<sup>5</sup> Available at [https://www.osc.gov.on.ca/en/SecuritiesLaw\\_91-506.htm](https://www.osc.gov.on.ca/en/SecuritiesLaw_91-506.htm)

<sup>6</sup> Available at <http://docs.mbsecurities.ca/msc/irp/en/item/101711/index.doc>

<sup>7</sup> Available at

[http://www2.publicationsduquebec.gouv.qc.ca/dynamicSearch/telecharge.php?type=3&file=/I\\_14\\_01/I14\\_01R0\\_1\\_A.HTM](http://www2.publicationsduquebec.gouv.qc.ca/dynamicSearch/telecharge.php?type=3&file=/I_14_01/I14_01R0_1_A.HTM)

<sup>8</sup> Available at <http://www.albertasecurities.com>, <http://www.bcsc.bc.ca>, <http://www.nbsc-cvmnb.ca>, <http://nssc.novascotia.ca> and <http://www.fcaa.gov.sk.ca/Securities%20Division>

apply to the Instrument. Accordingly, in Québec, *Regulation to amend Regulation 91-506 respecting Derivative Determination* is published by the *Autorité des marchés financiers* for consultation concurrently with the Proposed National Instrument.

## **VII. Anticipated Costs and Benefits**

The Proposed National Instrument seeks to ensure that the Canadian market for clearing customer OTC derivatives develops in a safe and efficient manner. It proposes a robust investor protection regime for Canadian clearing customers equivalent to the protections offered in major international markets and should also provide systemic benefits to the Canadian market. There will be compliance costs for clearing service providers that may increase the cost of clearing for market participants. In the Committee's view, the benefits to the Canadian market of implementing the Proposed National Instrument significantly outweigh the compliance costs to market participants. The major benefits and costs of the Proposed National Instrument are described below.

### ***(a) Benefits***

The two major benefits of the Proposed National Instrument are the reduction of systemic risk and the protection of customers and their assets when they indirectly clear OTC derivatives through clearing agencies.

#### ***(i) Mitigation of Systemic Risk***

The G20 has agreed that requiring standardized and sufficiently liquid OTC derivatives transactions to be cleared through central counterparties will result in more effective management of counterparty credit risk. In addition, the clearing of derivatives may also contribute to greater stability of our financial markets and to a reduction in systemic risk. The Proposed National Instrument is designed to create a framework for customer clearing that promotes stability of the OTC derivatives market by facilitating, to the greatest extent possible, the porting of customer positions and collateral. Portability of customer positions and related collateral is a key mechanism to ensure that in the event of a clearing intermediary default or insolvency, customer positions are not terminated and customer positions and collateral can be transferred to one or more non-defaulting clearing intermediaries without having to liquidate and re-establish a customer's positions. Portability can mitigate difficulties associated with stressed market conditions such as a market-wide reduction in liquidity and price dislocation, allow customers to maintain continuous clearing access and generally promotes efficient financial markets.

#### ***(ii) Customer Protection***

The Proposed National Instrument is aimed at significantly reducing the likelihood that customers will suffer major financial losses in the event of a clearing service provider's insolvency. In general, customer clearing offers risk mitigation benefits to customers. However, if a robust customer protection regime is not in effect, there can be risks in the indirect clearing process, particularly if a clearing intermediary becomes insolvent. The Proposed National Instrument provides customer protections that should significantly

reduce the likelihood of a range of negative potential consequences, that could occur in the event of a clearing intermediary's insolvency, including:

- forced liquidation of positions;
- loss or inaccessibility of collateral;
- loss of hedge positions necessitating re-entry into the market at time of stress to re-establish positions; and
- market uncertainty.

The Proposed National Instrument mitigates many of these risks to customers by establishing robust collateral and record keeping requirements. It requires customer positions to be fully collateralized at the regulated clearing agency and obligates the regulated clearing agency and clearing intermediaries to keep records that identify customers and their positions in order to facilitate porting.<sup>9</sup>

***(b) Costs***

Generally, any increased costs resulting from compliance with the Proposed National Instrument stem from enhanced collateral protection, record keeping and reporting requirements for customer collateral and positions. Any costs associated with complying with the Proposed National Instrument will be borne by clearing intermediaries and regulated clearing agencies and would likely be passed on to customers through higher initial margins and/or higher fees for transactions. There is also a possibility that clearing service providers may be dissuaded from entering or remaining in the Canadian market due to the costs of complying with the Proposed National Instrument reducing Canadian customers' options for clearing service providers.

***(i) Establishing Systems***

Clearing intermediaries and regulated clearing agencies will incur up-front costs to develop record-keeping and account structure systems required to comply with the Proposed National Instrument. However, once systems are established, the incremental cost of on-going compliance should be less significant.

***(ii) Loss of Potential Revenue for Clearing Intermediaries and Clearing Agencies***

The Instrument places restrictions on the use and investment of customer collateral held by clearing intermediaries and clearing agencies. Customer collateral may only be invested in liquid and low-risk instruments. The Instrument also requires a regulated

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<sup>9</sup> The level of protection afforded by the Proposed National Instrument is dependent on the Proposed National Instrument's interaction with other foreign and domestic laws such as bankruptcy and insolvency laws and the *Payment Clearing and Settlement Act* (Canada) as well as provincial and territorial personal property security laws including as they apply to cash collateral.

clearing agency to collect initial margin from clearing intermediaries for each customer on a gross basis. Gross margin promotes more effective porting of positions which benefits customers. However, this requirement means that less customer collateral will be held at and available for use by clearing intermediaries.<sup>10</sup> These requirements limit the potential revenue that clearing intermediaries and clearing agencies may earn through the use and investment of their customer's collateral.

### ***(iii) Market Access Issues***

Currently, OTC derivative clearing infrastructure and service providers are largely concentrated outside of Canada with the main clearing agencies and clearing intermediaries located in the United States and the European Union. Given the small size of the Canadian market there is a risk that the costs of analysing and complying with the Proposed National Instrument may result in some market participants choosing not to offer customer clearing in Canada which may limit Canadian customers' access to OTC derivative clearing services. However, as described above, the Committee is proposing substituted compliance for equivalently regulated foreign institutions and this could significantly reduce compliance costs associated with the Proposed National Instrument.

### ***(c) Conclusion***

Protection of customer positions and collateral is the fundamental principle of the Instrument. It is the Committee's view that the impact of the Proposed National Instrument, including anticipated compliance costs for market participants, is proportional to the benefits sought. The Instrument aims to provide a level of protection equal to that offered to customers in other jurisdictions. To achieve a balance of interests, the Proposed National Instrument is designed to deliver a high level of protection to customers transacting in OTC derivatives and create a safer environment in the Canadian market for customers to clear OTC derivatives, all while allowing clearing service providers a flexible and competitive market to operate in.

## **VIII. Contents of Annexes**

The following annexes form part of this CSA Notice:

- Annex A – Summary of Comments and List of Commenters;
- Annex B – Proposed National Instrument 94-102 *Derivatives: Customer Clearing and Protection of Customer Positions and Collateral*; and
- Annex C - Proposed Companion Policy 94-102CP *Derivatives: Customer Clearing and Protection of Customer Positions and Collateral*.

## **IX. Comments**

In addition to your comments on all aspects of the Instrument, the Committee also seeks specific feedback on the following question:

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<sup>10</sup> Clearing intermediaries would still have access to any excess collateral provided by customers.

Should clearing intermediaries be limited to clearing derivatives for local customers with regulated clearing agencies? Please explain what the impact of this limitation would be on your current clearing activities.

Please provide your comments in writing by **April 19, 2016**.

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 each of the Alberta Securities Commission at [www.albertasecurities.com](http://www.albertasecurities.com), the *Autorité des marchés financiers* at [www.lautorite.qc.ca](http://www.lautorite.qc.ca) and the Ontario Securities Commission at [www.osc.gov.on.ca](http://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:

Alberta Securities Commission  
Autorité des marchés financiers  
British Columbia Securities Commission  
Financial and Consumer Services Commission (New Brunswick)  
Financial and Consumer Affairs Authority of Saskatchewan  
Manitoba Securities Commission  
Nova Scotia Securities Commission  
Nunavut Securities Office  
Ontario 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  
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

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

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Autorité des marchés financiers  
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## Questions

Please refer your questions to any of:

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**ANNEX A**

**Summary of comments on *Model Provincial Rule – Derivatives: Customer Clearing and Protection of Customer Collateral and Positions***

<u>1. Issue/Reference</u>	<u>2. Summary of Comments</u>	<u>3. Response</u>
<b>GENERAL COMMENTS</b>		
<b>Harmonization of rules</b>	A number of commenters emphasized the importance of harmonizing the Canadian derivatives regime with international rules and standards.	The Committee agrees and is committed to implementing harmonized rules consistent with international standards. See also the substituted compliance section below.
	One commenter suggested that provincial rules should be consistent and implementation timelines should be coordinated to avoid regulatory arbitrage.	Change made. The Committee notes that it has now opted to develop a national instrument, given its intention that the substance of the Model Rule be the same across local jurisdictions and that market participants and derivative products receive the same treatment across Canada.
<b>Amendments to personal property security and bankruptcy regimes</b>	A number of commenters emphasized the importance of ensuring that personal property security and insolvency laws work with the Proposed National Instrument in order for Canadian participants to remain competitive on a global level.	The Committee is seeking to implement requirements which protect customer collateral, to the extent possible, under existing Canadian federal and provincial legal frameworks. The Committee notes that federal bankruptcy and provincial personal property security legislation are regimes which fall outside of the jurisdiction of the provincial securities regulatory authorities.
<b>Customer protection model</b>	Two commenters explained that the Model Rule is not compatible with the principal to principal model for customer clearing used in the European Union.  One commenter asked which customer protection regime is proposed to be implemented in Canada.	Multiple changes made. The Instrument now facilitates the offering of various models of customer clearing including the principal to principal model.

<p><b>Type of collateral accepted by a Derivatives Clearing Agency</b></p>	<p>A number of commenters suggested that the Committee should ensure that clearing agencies accept various types of Canadian collateral and/or increase the maximum amounts of such collateral they accept.</p>	<p>No change. The Committee recognizes the importance of Canadian clearing intermediaries and customers having the ability to utilize a broad range of collateral when posting collateral with a regulated clearing agency. Subject to the requirements and guidance provided in National Instrument 24-102 <i>Clearing Agency Requirements</i> and its companion policy, it is the Committee’s view that it should generally not prescribe the types of collateral a regulated clearing agency should accept, nor the limits it should place on that collateral. A request that a regulated clearing agency accept specific forms of collateral should be made by a clearing intermediary to the clearing agency, which would then go through its normal risk management process.</p>
<p><b>Substituted compliance</b></p>	<p>One commenter suggested that foreign-based recognized clearing agencies be permitted to comply by way of substituted compliance so as to avoid duplicative and onerous regulation.</p>	<p>The Committee will consider substituted compliance where a regulated clearing agency is subject to equivalent regulation. See Part V, subparagraph (b)(ii) of the Notice for a description of the Committee’s substituted compliance proposal.</p>
<p><b>PART 1: DEFINITIONS</b></p>		
<p><b>s. 1 – “clearing intermediary”</b></p>	<p>Two commenters suggested that the definition of “clearing intermediary” be expanded to include a scenario where there are multiple clearing intermediaries in a chain.</p> <p>One commenter suggested that financial intermediaries should be permitted to post collateral and meet reporting requirements on behalf of credit unions</p>	<p>Change made. The Instrument permits more than one clearing intermediary to be involved in a customer transaction.</p> <p>The Instrument does not prohibit clearing intermediaries from posting collateral on behalf of and fulfilling reporting requirements for their customers.</p>
<p><b>s. 1 – “customer collateral”</b></p>	<p>One commenter explained that the obligation to segregate variation margin is not possible for clearing agencies under certain customer protection models once the amount has been paid out to the clearing intermediary.</p>	<p>No change. Variation margin provided by a customer to its clearing intermediary is customer collateral and required to be segregated.</p>

<b>s. 1 – “excess margin”</b>	<p>One commenter suggested that the definition of “excess margin” be revised (i) to reflect that collateral is not excess margin until it is delivered to a clearing intermediary or clearing agency, and (ii) to clarify that any collateral delivered by a customer to a clearing agency or clearing intermediary which will be transformed should not be considered excess margin (i.e., it is the transformed collateral that is to be considered excess margin).</p>	<p>Change made. The definition has been revised to indicate that excess margin is customer collateral that has been delivered to a regulated clearing agency or clearing intermediary. Additionally, the CP has been revised to provide guidance clarifying that customer collateral initially delivered may be transformed and once transformed, only the transformed collateral is considered customer collateral and therefore excess margin.</p>
	<p>One commenter suggested that the definition be clarified to ensure that only collateral provided as margin for the customer’s derivatives is included in the definition. Specifically, the commenter was concerned that confusion would arise where a customer provided a security interest in various collateral in accordance with standard customer account documentation (e.g., a security interest in all securities accounts or a security interest in all present and after-acquired property) that was not being used as margin for its derivative transactions.</p> <p>Another commenter suggested that the definition should be expanded to include collateral that is delivered by a customer in excess of the amount required by a clearing agency for operational efficiencies.</p>	<p>Change made. The definition has been revised to specify that excess margin is collateral in respect of a customer’s cleared derivatives that is in excess of the amount of margin required by the regulated clearing agency to clear and settle such derivatives.</p>
<b>s. 1 – “permitted depository”</b>	<p>Two commenters suggested expanding the definition of “permitted depository” to include all entities through which collateral is currently being held by clearing agencies with global operations. Specifically, one commenter suggested expanding the definition to include securities settlement systems. The other commenter suggested that the definition should be broad enough to cover all potential securities intermediaries within an indirect holding system.</p>	<p>Change made. The definition in the Instrument covers various types of entities that are subject to a minimum amount of oversight required to ensure safekeeping of customer collateral including clearing intermediaries in the customer clearing chain that receive customer collateral. Other entities not covered by the definition may be granted an exemption on a case-by-case basis.</p>
<b>s. 1 – “permitted investment”</b>	<p>Two commenters suggested that minimum ratings (e.g., S&amp;P, DBRS, Moody’s) should be added as a requirement for an investment to be permitted and that the corresponding ratings be noted with the records of investment of customer collateral required under s. 23 of the Model Rule.</p>	<p>No change. The Committee has taken a principles based approach to permitted investments that does not rely on prescriptive requirements such as ratings.</p>

**PART 2: TREATMENT OF CUSTOMER COLLATERAL**

<b>s. 2 – Collection of initial margin</b>		
<b>General Comments</b>	Two commenters suggested that Canadian market participants should be given the choice to have initial margin requirements calculated in Canadian dollars.	No change. It is the Committee’s view that it is not appropriate to include a requirement that could introduce foreign exchange risk. If collateral is only calculated, but not accepted in Canadian dollars, this would not be a useful service because the calculation would not represent the currency required to be delivered.
<b>s. 2(1)</b>	One commenter suggested amending the Model Rule so that initial margin can be collected by either gross or net methods. Another commenter also requested the Model Rule be amended to permit netting of collateral requirements.	No change. There is a greater likelihood that customer positions may be under-margined when collected on a net-basis. However, the Committee has amended the Model Rule to allow excess margin to be used to secure or extend credit to a customer.
<b>s. 2(2)</b>	One commenter suggested that it is not necessary to include a requirement for a clearing intermediary to collect initial margin given that s. 6 of the Model Rule obligates a clearing intermediary to keep sufficient property with a clearing agency.	Change made. The section has been removed from the Instrument.
	One commenter suggested that it be clarified whether a clearing intermediary may use its own property to fund initial margin requirements set by a clearing agency.	No change. There is no prohibition in the Instrument against a clearing intermediary using its own property; however, any property provided must be treated as customer collateral.
<b>s. 3 – Segregation of customer collateral</b>		
<b>s. 3(2)</b>	Two commenters suggested that the Model Rule should allow the option for customers to request that customer collateral be held using the Full Physical Segregation Model.	No change. The Committee is of the view that the Full Physical Segregation Model may be more costly than its alternatives and may not materially improve the degree of protection for customers of a clearing intermediary and therefore, there is no requirement that a clearing agency offer the Full Physical Segregation model. However, a customer may privately contract with a clearing intermediary or regulated clearing agency for Full Physical Segregation.

s. 3(3)	Two commenters requested that the Model Rule not prohibit portfolio margining, and also requested that a mechanism for allowing portfolio margining be included.	No change. The Committee will continue to monitor developments in the market, and may make changes to the Proposed National Instrument, as necessary.
<b>s. 4 – Holding of customer collateral</b>		
<b>General Comments</b>	One commenter pointed out that Part 2 of the Model Rule permits commingling of customer collateral from multiple customers by clearing agencies and clearing intermediaries and that this seemed to contradict the requirement for individually segregated accounts to be held at a permitted depository. Additionally, two commenters suggested that the Model Rule should permit commingling of customer collateral.	Change made. Additional guidance has been added to the CP clarifying that customer collateral of multiple customers may be commingled in an omnibus customer account. The Instrument requires that the clearing intermediaries and clearing agencies identify the positions and collateral held for each individual customer within an omnibus customer account. Where a clearing intermediary or clearing agency deposits customer collateral with a permitted depository, the clearing intermediary or clearing agency is responsible for ensuring the permitted depository maintains appropriate books and records to ensure customer collateral can be attributed to each customer.
s. 4(3)	One commenter expressed concern regarding the requirement that all customer collateral be held in a segregated account that clearly identifies the name of each customer or otherwise indicates that the property in the account is customer collateral. The commenter’s concern was that this may jeopardize the absolute transfer characterization of cash in such circumstances.	Change made. The Instrument does not require that the name of each customer whose customer collateral is held at a permitted depository be identified on the account, provided that the account is identified as holding customer collateral.
<b>s. 6 – Clearing member maintenance of customer account balance</b>		
s. 6	Three commenters suggested clarifying that clearing agency margin calls are to take place once each day, and that clearing intermediaries will not be required to cure any customer collateral shortfall on a continuous basis.	No change. The clearing intermediary will be required to meet the margin requirements of the clearing agency within the time limits set out by the clearing agency.

<b>s. 8 – Use of customer collateral</b>		
<b>s. 8</b>	One commenter expressed the view that market participants should have the right to contract in respect of excess collateral as they deem appropriate without restriction, and thus that the Model Rule should expressly allow the re-hypothecation of excess margin to the extent it is held by a clearing agency or clearing intermediary.	Change made. The Instrument has been revised to articulate that customer collateral may be bought or sold pursuant to an agreement for resale or repurchase under prescribed conditions.
	One commenter suggested that the Model Rule should expressly allow a clearing intermediary or a clearing agency to offer collateral transformation services to the customer.	Change made. The CP explains that collateral transformation is acceptable and transformed collateral would be considered customer collateral.
	One commenter noted that the CFTC’s rules expressly provide for the right to withdraw customer collateral from a customer account to margin, guarantee, secure, transfer, adjust or settle the customer’s cleared transactions and requested that the Model Rule make this point distinctly.	Change made. The language in the Instrument expressly grants this right.
	One commenter noted that margin held at the clearing intermediary level should be permitted to secure other obligations of the customer to the clearing intermediary.	Change made. Excess margin held by a clearing intermediary may be used to secure or extend credit to the customer.
<b>s. 9 – Investment of customer collateral</b>		
<b>s. 9(1)</b>	One commenter suggested that customers should be permitted to restrict how customer collateral is invested.	No change. The Instrument restricts investment of customer collateral to conservative investments (determined using a principles-based approach) and it is the Committee’s view that further restrictions should be a private contractual matter between customers and clearing intermediaries or clearing agencies.
	One commenter suggested that a requirement to report all losses and gains made on investments of customer collateral be added to the Model Rule.	No change. Section 26 of the Instrument requires that the customer receive a daily report setting out the current value of customer collateral. This report includes any daily changes in the value of invested customer collateral.

s. 9(2)	One commenter expressed concern that a clearing intermediary may be liable for the losses that result from collateral that is transformed for the customer.	Change made. The CP clarifies that investment losses relate only to investments made by a regulated clearing agency or clearing intermediary using customer collateral, not to the collateral that is transformed for a customer.
	One commenter suggested that the Model Rule allow any investment losses incurred by a clearing agency to be mutualised and allocated to clearing intermediaries.	Change made. The CP explains that investment losses incurred by a regulated clearing agency may be mutualised and allocated to clearing intermediaries, but not to customers.
<b>s. 10 – Acting as a clearing intermediary</b>		
s. 10	One commenter suggested that a clearing agency should not be required to approve the clearing intermediary’s customers. Instead, a clearing agency should be allowed to request information about customers and to refuse access to clearing services to a customer of a clearing intermediary.	Change made. A regulated clearing agency is no longer required to approve indirect intermediaries and customers.
<b>s. 13 – Same</b>		
s. 13	Two commenters requested clarification on what is meant by “prudentially regulated” and “appropriate regulatory authority”.	Change made. The CP clarifies that, in Canada, prudential regulation of federally regulated financial institutions is undertaken by the Office of the Superintendent of Financial Institutions. Other regulators that perform prudential oversight include the Investment Industry Regulatory Organization of Canada and certain provincial prudential market regulators, such as the Autorité des marchés financiers in Québec or other local securities regulatory authorities. An appropriate foreign regulatory authority would be one that applies comparable regulatory standards to those applied to Canadian entities.

<b>PART 3: RECORD-KEEPING</b>		
<b>s.16 – Retention of records</b>		
<b>s.16</b>	One commenter requested that this requirement not apply to clearing agencies that are exempt from recognition under s. 147 of the <i>Securities Act</i> (Ontario).	No change. Retention of records is a requirement for all regulated clearing agencies and clearing intermediaries falling within the scope of the Instrument. However, substituted compliance may be available. See the substituted compliance section above.
<b>s. 17 – Books and records</b>		
<b>s. 17(4)</b>	One commenter suggested removing the word “market” from “market value” to provide for a wider range of alternatives when calculating customer collateral held.	Change made. The word “market” has been removed to ensure that other accepted types of valuation methodologies can be utilized, where appropriate.
<b>s. 20 – Separate records – derivatives clearing agency</b>		
<b>s. 20</b>	One commenter suggested that the Model Rule should require clearing agencies to keep records of the positions and property of each customer only where the customer is a direct customer of a clearing intermediary, and therefore, identifiable to the clearing agency. The commenter also suggested that the Model Rule should allow clearing agencies to keep records of the positions and property of each clearing intermediary's customers at an aggregate level per clearing intermediary.	No change. Without records for customers clearing through clearing intermediaries, portability would be impeded.
<b>PART 4: REPORTING AND DISCLOSURE</b>		
<b>General Comments</b>	Two commenters expressed concern over confidentiality and public access to the customer collateral reports.	Reports will be treated as confidential by securities regulatory authorities, subject to applicable provisions of the freedom of information and protection of privacy legislation adopted by each province and territory. However, the Committee may share the reports with self-regulatory organizations or other relevant regulatory authorities.

<b>s. 25 – Disclosure to clearing members and customers</b>		
<b>s. 25(4)</b>	Two commenters expressed concern over the requirement to receive written acknowledgements from customers and one of the commenters suggested to either make the disclosure publicly available or incorporate the disclosure into the legal agreements between the parties.	Change made. The requirement to receive written acknowledgements from customers has been removed.
<b>s. 28 – Customer collateral report</b>		
<b>s. 28(3) and s. 28(4)</b>	One commenter requested that this requirement not apply to clearing agencies that are exempt from recognition under s. 147 of the <i>Securities Act</i> (Ontario). Another commenter suggested that the requirements under these subsections should not apply to foreign-based recognized clearing agencies and instead they should be permitted to comply by way of substituted compliance.	No change. See the substituted compliance section above. The Committee would consider foreign reporting requirements in our substituted compliance analysis. However, the information contained in the reports is necessary in order for the securities regulatory authorities to fulfill their mandates.
<b>s. 28(5)</b>	One commenter requested clarification on whether the reporting requirement applies in respect of (a) each individual derivatives transaction or an aggregate net exposure for all derivatives transactions for a customer, and (b) each individual type of customer collateral or collateral on an aggregate basis, regardless of collateral type. The commenter also suggested that the Model Rule should be revised to include asset type and quantity (in addition to the market value) of customer collateral that is posted by a clearing intermediary to a clearing agency on behalf of a customer.	Change made. The reporting requirement is intended to be applied in respect of aggregate net exposures for all derivatives transactions of each customer. The Instrument requires clearing intermediaries to report the current value, asset type and quantity of the collateral received.
<b>s. 29 – Disclosure of customer collateral investment</b>		
<b>s. 29(1)</b>	One commenter expressed concern over inadvertently requiring a clearing agency to publicly disclose proprietary information such as its investment guidelines and policies.	Change made. Regulated clearing agencies are only required to disclose their investment guidelines and policies directly to the customer and, if applicable, a direct intermediary.
<b>s. 29(2)</b>	One commenter expressed concern over the onerous requirement to receive written acknowledgements from customers and suggested that disclosure be incorporated into the legal agreements between the parties.	Change made. See response to comments on s. 25(4).

s. 29(3)	Two commenters noted that the timing for submitting the required report is not specified.	Change made. Monthly reporting to securities regulatory authorities on customer collateral is required to be delivered within 10 business days of the end of each calendar month.
<b>PART 5: TRANSFER OF POSITIONS</b>		
<b>General Comments</b>	One commenter noted that a clearing agency may not be in a position to ascertain whether or not a customer is in default and suggested that the provisions of this section be revised to reflect the solvency status of the customer's account (i.e., whether or not the collateral value is sufficient to cover the initial margin obligations).	Change made. The Instrument now provides that a regulated clearing agency and a direct intermediary may facilitate porting of a customer's positions and collateral only where the customer's account is not currently in default.
<b>s. 30 - Transfer of customer collateral and positions</b>		
s. 30(1)	One commenter suggested changing the language of the subsection from "transfer of the customer's positions and customer collateral" to "transfer of the customer's positions and customer collateral or its liquidation proceeds".	Change made. The Instrument now permits transfer of the liquidation proceeds of customer collateral.
	One commenter requested clarification on when a clearing intermediary that is to receive transferred customer positions and collateral, or its liquidation proceeds, provides its consent to the transfer (i.e., if consent would be provided pursuant to arrangements made between parties at the outset of the relationship or concurrently with an event of default).	Change made. Additional guidance has been provided in the CP setting out that it is the Committee's view that such consent for transfer should be obtained at the outset of the clearing relationship.
s. 30(3)	One commenter suggested adding a requirement that conditions (a) to (e) be met within a reasonable time that is to be predetermined by a clearing agency.	No change; however, the Committee has provided additional guidance in the CP with respect to the timing for customers and direct intermediaries to provide consent to a transfer.

**List of Commenters:**

1. Atlantic Central
2. Caisse de dépôt et placement du Québec
3. Canadian Investor Protection Fund
4. Canadian Life and Health Insurance Association Inc.
5. Canadian Market Infrastructure Committee
6. Capital Power Corporation
7. Central 1 Credit Union
8. Concentra Financial Services
9. Enbridge Inc.
10. ICE Clear Credit LLC
11. IGM Financial Inc.
12. International Swaps and Derivatives Association, Inc.
13. Investment Industry Association of Canada
14. LCH.Clearnet Group Limited
15. NB Investment Management Corp.
16. Pension Investment Association of Canada
17. RBC Global Asset Management Inc.
18. SaskEnergy Incorporated
19. Suncor Energy
20. The Canadian Commercial Energy Working Group
21. TMX Group Limited
22. TransCanada Corp.

## ANNEX B

### NATIONAL INSTRUMENT 94-102 *DERIVATIVES: CUSTOMER CLEARING AND PROTECTION OF CUSTOMER COLLATERAL AND POSITIONS*

#### PART 1 DEFINITIONS, INTERPRETATION AND APPLICATION

##### Definitions and Interpretation

1. (1) In this Instrument,

“Canadian financial institution” means a Canadian financial institution as defined in National Instrument 45-106 *Prospectus Exemptions*;

“cleared derivative” means a transaction in a derivative that is, directly or indirectly, submitted to and cleared by a clearing agency;

“clearing intermediary” means a direct intermediary or an indirect intermediary;

“customer” means a counterparty to a cleared derivative other than a clearing intermediary or a regulated clearing agency;

“customer collateral” means all cash, securities and other property if either of the following applies:

- (a) they are received or held by a clearing intermediary or regulated clearing agency from, for or on behalf of a customer, and are intended to or does margin, guarantee, secure, settle or adjust a cleared derivative of the customer;
- (b) they are deposited on behalf of a customer by a clearing intermediary to satisfy the margin requirements of the customer’s cleared derivatives at a regulated clearing agency;

“direct intermediary” means a person or company that

- (a) with respect to a cleared derivative, is a participant of the regulated clearing agency at which the cleared derivative is cleared,
- (b) provides clearing services for a customer in respect of a cleared derivative entered into by, for or on behalf of the customer, and
- (c) requires, receives or holds collateral from, for or on behalf of the customer in providing clearing services;

“excess margin” means customer collateral in respect of a customer’s cleared derivatives that

- (a) is delivered to a regulated clearing agency or clearing intermediary from, for or on behalf of the customer, and
- (b) has a value in excess of the amount required by the regulated clearing agency to clear and settle the cleared derivatives of the customer;

“indirect intermediary” means a person or company that

- (a) provides indirect clearing services for a customer in respect of a cleared derivative entered into by, for or on behalf of the customer, and
- (b) requires, receives or holds collateral from, for or on behalf of the customer in providing clearing services;

“initial margin” means, in relation to a regulated clearing agency’s margin system that manages credit exposures to its participants, collateral that is required by the regulated clearing agency to cover potential changes in the value of a customer’s cleared derivatives positions over an appropriate close-out period in the event of default;

“local customer” means a customer that, in respect of a local jurisdiction, is either of the following:

- (a) an individual who is resident in the local jurisdiction;
- (b) a person or company to which one or more of the following applies:
  - (i) it is organized or incorporated under the laws of the local jurisdiction;
  - (ii) its head office is in the local jurisdiction;
  - (iii) its principal place of business is in the local jurisdiction;

“participant” means a person or company that has entered into an agreement with a regulated clearing agency to access the services of the regulated clearing agency and is bound by the regulated clearing agency’s rules and procedures;

“permitted depository” means a person or company that is any of the following:

- (a) a Canadian financial institution or Schedule III bank;
- (b) a regulated clearing agency;
- (c) a foreign entity that
  - (i) is incorporated or organized under the laws of a permitted jurisdiction,

- (ii) is regulated as a banking institution or trust company by the government, or an agency of the government, of a permitted jurisdiction, and
  - (iii) has shareholders' equity, as reported in its most recent audited financial statements, of not less than the equivalent of \$100,000,000;
- (d) either of the following, but only with respect to customer collateral that it receives from a customer or a clearing intermediary for which it provides clearing services:
- (i) a registered investment dealer as defined in National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*;
  - (ii) a prudentially regulated foreign entity, other than a foreign entity listed in paragraph (c) that is registered, licensed or otherwise permitted to perform the services of a clearing intermediary in accordance with the laws and regulations of a permitted jurisdiction;

“permitted investment” means cash or a highly liquid financial instrument with minimal market and credit risk that is capable of being liquidated rapidly with minimal adverse price effect;

“permitted jurisdiction” means a foreign jurisdiction that is any of the following:

- (a) a country where the primary regulator of a Schedule III bank is located, or a political subdivision thereof;
- (b) if a customer has provided express written consent to a cleared derivative in a foreign currency, the country of origin of the foreign currency used to denominate the rights and obligations under the cleared derivative entered into by, for or on behalf of the customer, or a political subdivision thereof;
- (c) a jurisdiction approved by the regulator or the securities regulatory authority from time to time, subject to such conditions or restrictions as may be imposed in the approval;

“qualifying central counterparty” means an entity to which each of the following applies:

- (a) it is licensed to operate as a central counterparty in a jurisdiction of Canada or a foreign jurisdiction by a government or regulatory authority;
- (b) it is subject to regulation that is generally consistent with the *Principles for market infrastructures* published by the Bank for International Settlements' Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions in April 2012, as amended from time to time;

“regulated clearing agency” means

- (a) in British Columbia, Manitoba, Ontario and Saskatchewan, a person or company recognized or exempted from recognition as a clearing agency in the local jurisdiction,
- (b) in Québec, a person recognized or exempted from recognition as clearing house or as a central securities depository under the Securities Act (Québec), and
- (c) in Alberta, Newfoundland and Labrador, New Brunswick, the Northwest Territories, Nova Scotia, Nunavut, Prince Edward Island and Yukon, a person or company recognized or exempted from recognition as a clearing agency or clearing house pursuant to the securities legislation of any jurisdiction of Canada;

“Schedule III bank” means an authorized foreign bank named in Schedule III of the *Bank Act* (Canada);

“segregate” means to separately hold or account for customer collateral and customer positions;

“transaction” means any of the following:

- (a) entering into a derivative or making a material amendment to, terminating, assigning, selling or otherwise acquiring or disposing of a derivative;
- (b) the novation of a derivative, other than a novation with a clearing agency.

**(2)** In this Instrument, a person or company is an affiliated entity of another person or company if one of them controls the other or each of them is controlled by the same person or company.

**(3)** In this Instrument, a person or company (the first party) is considered to control another person or company (the second party) if any of the following apply:

- (a) the first party beneficially owns or directly or indirectly exercises control or direction over securities of the second party carrying votes which, if exercised, would entitle the first party to elect a majority of the directors of the second party, unless the first party holds the voting securities only to secure an obligation;
- (b) the second party is a partnership, other than a limited partnership, and the first party holds more than 50% of the interests of the partnership;
- (c) the second party is a limited partnership and the general partner of the limited partnership is the first party.

## **Application**

2. (1) This Instrument applies to all of the following:

- (a) a regulated clearing agency located in a local jurisdiction that clears a cleared derivative entered into by, for or on behalf of a customer;
- (b) a regulated clearing agency located in a foreign jurisdiction that clears a cleared derivative entered into by, for or on behalf of a local customer, but only in respect of that derivative;
- (c) a clearing intermediary that provides clearing services for a cleared derivative entered into by, for or on behalf of a local customer, but only in respect of that derivative.

(2) This Instrument applies to each of the following:

- (a) in Manitoba, a derivative as prescribed in Manitoba Securities Commission Rule 91-506 *Derivatives: Product Determination*;
- (b) in Ontario, a derivative as prescribed in Ontario Securities Commission Rule 91-506 *Derivatives: Product Determination*;
- (c) in Québec, a derivative as specified in Regulation 91-506 respecting derivatives determination.

(3) In Alberta, British Columbia, New Brunswick, Newfoundland and Labrador, the Northwest Territories, Nova Scotia, Nunavut, Prince Edward Island, Saskatchewan and Yukon, in this Instrument, each reference to a “derivative” is a reference to a specified derivative as defined in Multilateral Instrument 91-101 *Derivatives: Product Determination*.

## **PART 2**

### **TREATMENT OF CUSTOMER COLLATERAL BY A CLEARING INTERMEDIARY**

#### **Segregation of customer collateral – clearing intermediary**

3. (1) A clearing intermediary must segregate customer collateral from the property of other persons or companies including the property of the clearing intermediary.
- (2) A clearing intermediary must segregate the customer collateral of the customer of an indirect intermediary from any property of the indirect intermediary.

#### **Holding of customer collateral – clearing intermediary**

4. A clearing intermediary must hold all customer collateral in one or more accounts at a permitted depository and clearly identify such accounts as holding customer collateral.

### **Excess margin – clearing intermediary**

5. A clearing intermediary must have rules, policies or procedures in place with respect to identifying and recording, at least once each business day, the value of excess margin that it holds that is attributable to each customer for which the clearing intermediary provides clearing services.

### **Use of customer collateral – clearing intermediary**

6. (1) A clearing intermediary must not use or permit the use of customer collateral except in accordance with this section and sections 7 and 8.
  - (2) A clearing intermediary may use or permit the use of customer collateral of a customer to do either of the following:
    - (a) margin, guarantee, secure, settle or adjust cleared derivatives of the customer;
    - (b) with respect to excess margin, secure or extend the credit of the customer.
  - (3) Other than with respect to excess margin used in accordance with paragraph (2)(b), a clearing intermediary must not impose or permit the imposition of a lien or claim on a customer's positions or customer collateral except to secure a claim resulting from a cleared derivative in favour of any of the following:
    - (a) the customer;
    - (b) the regulated clearing agency or clearing intermediary responsible for clearing the cleared derivatives of the customer to which the positions or customer collateral relate.

### **Investment of customer collateral – clearing intermediary**

7. (1) A clearing intermediary must not invest customer collateral except in accordance with subsection (2).
  - (2) Subject to subsection (3), a clearing intermediary may
    - (a) invest property received as customer collateral in a permitted investment, and
    - (b) use customer collateral to buy or sell a permitted investment pursuant to an agreement for resale or repurchase if all of the following apply:
      - (i) the agreement is in writing;
      - (ii) the term of the agreement is no more than one business day;
      - (iii) written confirmation specifying the terms of the agreement is delivered to the customer immediately upon entering into the transaction;

(iv) the agreement is not entered into with an affiliated entity of the clearing intermediary.

- (3) A loss resulting from an investment of customer collateral by the clearing intermediary must be borne by the clearing intermediary making the investment and not by the customer.

#### **Use of customer collateral - indirect intermediary default**

8. (1) Except as provided in subsection (2), a clearing intermediary must not apply customer collateral of a customer of an indirect intermediary for which the clearing intermediary provides clearing services to satisfy the obligations of that indirect intermediary.

(2) A clearing intermediary may apply the customer collateral of a customer in full or partial satisfaction of an indirect intermediary's obligations that arise or are accelerated as a consequence of the indirect intermediary's default only to the extent that those obligations are attributable to the cleared derivatives of the customer.

#### **Acting as a clearing intermediary**

9. (1) A person or company must not provide clearing services for a customer as a clearing intermediary unless the person or company is one of the following:

- (a) prudentially regulated by an appropriate regulatory authority in Canada;
- (b) prudentially regulated by an appropriate regulatory authority in a permitted jurisdiction and registered, licensed or otherwise permitted to perform the services of a clearing intermediary in accordance with the laws and regulations of that permitted jurisdiction.

(2) A clearing intermediary must not provide clearing services for a customer unless the clearing services are provided in respect of derivatives that are cleared through

- (a) except in Alberta, a regulated clearing agency, and
- (b) in Alberta, a regulated clearing agency or a qualifying central counterparty.

#### **Risk management – clearing intermediary**

10. A clearing intermediary that provides or proposes to provide clearing services for an indirect intermediary must have rules, policies or procedures reasonably designed to

- (a) identify, monitor and manage material risks arising from the provision of clearing services, and
- (b) manage a default of the indirect intermediary.

### **Risk management – indirect intermediary**

11. (1) An indirect intermediary must have rules, policies or procedures reasonably designed to identify, monitor and manage the material risks arising from the provision of indirect clearing services for a customer.
- (2) An indirect intermediary that receives clearing services by a clearing intermediary must provide the clearing intermediary with all information reasonably required to identify, monitor and manage any material risks arising from the provision of indirect clearing services for customers.

## **PART 3 RECORD KEEPING BY A CLEARING INTERMEDIARY**

### **Retention of records – clearing intermediary**

12. A clearing intermediary must keep the records required under this Part and Part 4, and all supporting documentation, in a readily accessible location for at least 7 years after the date upon which the cleared derivative expires or terminates.

### **Books and records – clearing intermediary**

13. (1) A clearing intermediary that receives customer collateral must calculate and record all of the following, at least once each business day, in its books and records for each customer:
- (a) the amount of customer collateral it requires from, for or on behalf of each customer;
  - (b) the total amount of customer collateral it requires from, for or on behalf of all customers.
- (2) For each indirect intermediary that a clearing intermediary provides clearing services for, the clearing intermediary must calculate and record all of the following, at least once each business day:
- (a) the amount of customer collateral it requires from, for or on behalf of each customer of each indirect intermediary;
  - (b) the total amount of customer collateral it requires from, for or on behalf of all customers of each indirect intermediary.
- (3) A clearing intermediary must record all of the following in its books and records for each customer:
- (a) each permitted depository at which it holds customer collateral of the customer;
  - (b) a description of the customer collateral held at each permitted depository;

- (c) the current value of any customer collateral received from, for or on behalf of the customer, including, without limitation, all of the following at least once each business day:
- (i) any accruals on the customer collateral creditable to the customer;
  - (ii) any gains or losses in respect of the customer collateral;
  - (iii) any charges lawfully accruing to the customer;
  - (iv) any distributions or transfers of the customer collateral.

#### **Books and records – direct intermediary**

14. A direct intermediary must record all of the following, at least once each business day, in its books and records for each customer:
- (a) the total amount of customer collateral required for the cleared derivatives of the customer by each regulated clearing agency;
  - (b) the total amount of the customer's excess margin held by the direct intermediary.

#### **Books and records – indirect intermediary**

15. An indirect intermediary must record all of the following, at least once each business day, in its books and records for each customer:
- (a) the total amount of collateral required for the cleared derivatives of the customer by each clearing intermediary through which the indirect intermediary clears;
  - (b) the aggregate sum of the amounts in paragraph (a);
  - (c) the total amount of the customer's excess margin held by the indirect intermediary.

#### **Separate records – direct intermediary**

16. A direct intermediary must keep separate books and records that, at any time, enable it to distinguish all of the following in its own accounts and in the accounts held with the regulated clearing agency:
- (a) the positions and property of the direct intermediary;
  - (b) the positions and value of customer collateral held for or on behalf of each of the direct intermediary's customers.

### **Separate records – indirect intermediary**

17. An indirect intermediary must keep separate books and records that, at any time, enable it to distinguish all of the following in its own accounts and in the accounts held with each clearing intermediary through which it provides clearing services:
- (a) the positions and property of the indirect intermediary;
  - (b) the positions and value of customer collateral held for or on behalf of each of the indirect intermediary's customers.

### **Separate records – multiple clearing intermediaries**

18. A clearing intermediary that provides clearing services in respect of a cleared derivative for an indirect intermediary must keep separate books and records that, at any time, enable it and each of its indirect intermediaries to distinguish all of the following in the accounts held with the clearing intermediary:
- (a) the positions and property of the indirect intermediary;
  - (b) the positions and value of customer collateral held for, or on behalf of the indirect intermediary's customers.

### **Records of investment of customer collateral – clearing intermediary**

19. A clearing intermediary that invests customer collateral must keep records of all of the following with respect to each investment of customer collateral:
- (a) the date of the investment;
  - (b) the name of each person or company through which the investment was made;
  - (c) a daily market valuation of the investment, any unrealized gain or loss on that investment and related supporting documentation;
  - (d) a description of each asset or instrument in which the investment was made;
  - (e) the identity of each permitted depository where each asset, as applicable, or instrument is deposited;
  - (f) the date on which the investment was liquidated or otherwise disposed of and the realized gain or loss;
  - (g) the name of each person or company liquidating or disposing of the investment.

### **Records of currency conversion – clearing intermediary**

20. A clearing intermediary must keep a record of each conversion of customer collateral from one currency to another.

**PART 4**  
**REPORTING AND DISCLOSURE BY A CLEARING INTERMEDIARY**

**Clearing intermediary delivery of disclosure by regulated clearing agency**

- 21.** Before receiving the first cleared derivative from, for or on behalf of a customer, a clearing intermediary must provide the customer, or an indirect intermediary for which it provides clearing services, with all of the following:
- (a) the written disclosure provided under section 41 by each regulated clearing agency through which the direct intermediary clears a transaction for the customer or indirect intermediary;
  - (b) the investment guidelines and policy and any changes to such investment guidelines and policy provided under section 45 by each regulated clearing agency that invests customer collateral attributable to the customer.

**Disclosure to customer by clearing intermediary**

- 22. (1)** Before receiving the first cleared derivative from, for or on behalf of a customer, a clearing intermediary must provide written disclosure to the customer describing the treatment of customer collateral not held at a regulated clearing agency, including the impact of relevant bankruptcy and insolvency laws, in the event of a default by the clearing intermediary.
- (2)** After accepting the first cleared derivative from, for or on behalf of a customer of, each time there is a change to the treatment of customer collateral not held at a regulated clearing agency, the clearing intermediary must provide written disclosure to the customer, within a reasonable period of time, describing the change.

**Disclosure to customer by indirect intermediary**

- 23. (1)** Before receiving the first cleared derivative from, for or on behalf of a customer, an indirect intermediary must provide written disclosure including a description of all of the following to the customer:
- (a) the risks associated with receiving clearing services through an indirect intermediary;
  - (b) the rules, policies or procedures for transferring positions and customer collateral, in the event of the indirect intermediary's default, to another clearing intermediary.
- (2)** After accepting the first cleared derivative from, for or on behalf of a customer of, each time there is a change to the rules, policies or procedures referred to in paragraph (1)(b), the indirect intermediary must provide written disclosure to the customer, within a reasonable period of time, describing the change made to the rules, policies or procedures.

## **Customer information – clearing intermediary**

**24. (1)** A direct intermediary must provide all of the following to a regulated clearing agency:

- (a) before submitting to the regulated clearing agency the first cleared derivative for or on behalf of a customer of the direct intermediary, or of an indirect intermediary for which the direct intermediary provides clearing services, information sufficient to identify the customer and the customer's positions and customer collateral;
- (b) at least once each business day after providing the information referred to in paragraph (a), information that identifies the customer's positions and customer collateral.

**(2)** An indirect intermediary must provide all of the following to a clearing intermediary through which it provides clearing services:

- (a) before submitting to the clearing intermediary the first cleared derivative for or on behalf of a customer, information sufficient to identify the customer and the customer's positions and customer collateral;
- (b) at least once each business day after providing the information referred to in paragraph (a), information that identifies the customer's positions and customer collateral.

## **Customer collateral report - regulatory**

**25. (1)** A direct intermediary that receives customer collateral must electronically submit to the regulator or securities regulatory authority, within 10 business days of the end of each calendar month, a completed Form 94-102F1 *Customer Collateral Report: Direct Intermediary*.

**(2)** An indirect intermediary that receives customer collateral must electronically submit to the regulator or securities regulatory authority, within 10 business days of the end of each calendar month, a completed Form 94-102F2 *Customer Collateral Report: Indirect Intermediary*.

## **Customer collateral report - customer**

**26. (1)** A clearing intermediary must make available to each customer from, for or on behalf of whom it receives customer collateral, a report, calculated and available on a daily basis, setting out all of the following:

- (a) the current value of the cleared derivative positions of the customer;
- (b) the current value, asset type and quantity of customer collateral received from, for or on behalf of the customer that is held by the clearing intermediary and the location of each permitted depository at which the customer collateral is held;
- (c) the current value of the customer collateral received from, for or on behalf of the customer that is posted with any of the following:

- (i) a regulated clearing agency;
  - (ii) another clearing intermediary.
- (2) A clearing intermediary must make available to each indirect intermediary from which it receives customer collateral for or on behalf of a customer, a report, calculated and available on a daily basis, setting out all of the following:
  - (a) the current value of the cleared derivative positions of the customer;
  - (b) the current value, asset type and quantity of customer collateral received from the indirect intermediary on behalf of the customer that is held by the clearing intermediary and the location of each permitted depository at which the customer collateral is held;
  - (c) the current value of the customer collateral received from the indirect intermediary on behalf of the customer that is posted with any of the following:
    - (i) a regulated clearing agency;
    - (ii) another clearing intermediary.

#### **Disclosure of investment of customer collateral**

- 27. (1) Before receiving the first cleared derivative from, for or on behalf of a customer, a clearing intermediary that invests customer collateral must disclose in writing its investment guidelines and policy directly to the customer, or, if applicable, to the indirect intermediary that is providing clearing services to the customer.
- (2) A clearing intermediary that invests customer collateral must promptly disclose in writing any change to its investment guidelines and policy directly to the customer, or, if applicable, to the indirect intermediary that is providing clearing services to the customer.

### **PART 5 TREATMENT OF CUSTOMER COLLATERAL BY A REGULATED CLEARING AGENCY**

#### **Collection of initial margin**

- 28. A regulated clearing agency must collect initial margin for each customer on a gross basis.

#### **Segregation of customer collateral – regulated clearing agency**

- 29. A regulated clearing agency must segregate customer collateral from the property of other persons or companies including the property of the regulated clearing agency.

### **Holding of customer collateral – regulated clearing agency**

- 30. (1)** A regulated clearing agency must hold all customer collateral in one or more accounts at a permitted depository and clearly identify such accounts as holding customer collateral.
- (2)** A regulated clearing agency must hold all customer collateral of each customer separately from all other property of such customer that is not customer collateral.

### **Excess margin – regulated clearing agency**

- 31.** A regulated clearing agency must have rules, policies or procedures in place with respect to identifying and recording, at least each business day, the value of excess margin that it holds for or on behalf of each customer.

### **Use of customer collateral – regulated clearing agency**

- 32. (1)** A regulated clearing agency must not use or permit the use of customer collateral except in accordance with this section and sections 33 and 34.
- (2)** A regulated clearing agency may use or permit the use of customer collateral of a customer to do either of the following:
- (a)** margin, guarantee, secure, settle or adjust cleared derivatives of the customer;
  - (b)** with respect to excess margin, secure or extend the credit of the customer.
- (3)** Other than with respect to excess margin used in accordance with paragraph (2)(b), a regulated clearing agency must not impose or permit the imposition of a lien or claim on a customer's positions or customer collateral except to secure a claim resulting from a cleared derivative in favour of any of the following:
- (a)** the customer;
  - (b)** the regulated clearing agency or a clearing intermediary responsible for clearing the cleared derivatives of the customer to which the positions or customer collateral relate.

### **Investment of customer collateral – regulated clearing agency**

- 33. (1)** A regulated clearing agency must not invest customer collateral except in accordance with subsection (2).
- (2)** Subject to subsection (3), a regulated clearing agency may
- (a)** invest property received as customer collateral in a permitted investment, and
  - (b)** use customer collateral to buy or sell a permitted investment pursuant to an agreement for resale or repurchase to which all of the following apply:
    - (i)** the agreement is in writing;

- (ii) the term of the agreement is no more than one business day;
  - (iii) written confirmation specifying the terms of the agreement is delivered to the customer immediately upon entering into the transaction;
  - (iv) the agreement is not entered into with an affiliated entity of the regulated clearing agency.
- (3) Any loss resulting from an investment of customer collateral by the regulated clearing agency must be borne by the regulated clearing agency making the investment and not by any customer.

#### **Use of customer collateral - clearing intermediary default**

34. (1) Except as otherwise provided in subsection (2), a regulated clearing agency must not apply customer collateral to satisfy the obligations of a clearing intermediary to which the regulated clearing agency provides clearing services.
- (2) A regulated clearing agency may apply the customer collateral of a customer in full or partial satisfaction of a clearing intermediary's obligations that arise or are accelerated as a consequence of the clearing intermediary's default only to the extent that those obligations are attributable to the cleared derivatives of the customer.

#### **Risk management –NI 24-102 applies**

35. Part 3 of National Instrument 24-102 *Clearing Agency Requirements* apply to a regulated clearing agency and, for that purpose, a reference in that instrument to a “recognized clearing agency” is to be read as a reference to a “regulated clearing agency”.

### **PART 6 RECORD KEEPING BY A REGULATED CLEARING AGENCY**

#### **Retention of records – regulated clearing agency**

36. A regulated clearing agency must keep the records required under this Part and Part 7, and all supporting documentation, in a readily accessible location for at least 7 years after the date upon which the cleared derivative expires or terminates.

#### **Books and records – regulated clearing agency**

37. (1) A regulated clearing agency that receives customer collateral must calculate and record all of the following, at least once each business day, in its books and records for each customer:
- (a) the amount of customer collateral it requires from, for or on behalf of each customer;

- (b) the total amount of customer collateral it requires from, for or on behalf of all customers.
- (2) A regulated clearing agency must record all of the following in its books and records for each customer:
- (a) each permitted depository at which it holds customer collateral of the customer;
  - (b) a description of the customer collateral held at each permitted depository;
  - (c) the current value of any customer collateral received from, for or on behalf of the customer, including, without limitation, all of the following at least once each business day:
    - (i) any accruals on the customer collateral creditable to the customer;
    - (ii) any gains or losses in respect of the customer collateral;
    - (iii) any charges lawfully accruing to the customer;
    - (iv) any distributions or transfers of the customer collateral.

#### **Separate records – regulated clearing agency**

38. A regulated clearing agency must keep separate books and records that, at any time, enable it and each of its direct intermediaries to distinguish all of the following in the accounts held at the regulated clearing agency:
- (a) the positions and property held for the account of the direct intermediary;
  - (b) the positions and value of customer collateral held for or on behalf of the direct intermediary's customers;
  - (c) the positions and value of customer collateral held for or on behalf of customers of each indirect intermediary for which the direct intermediary provides clearing services.

#### **Records of investment of customer collateral – regulated clearing agency**

39. A regulated clearing agency that invests customer collateral must keep records of all of the following with respect to each investment of customer collateral:
- (a) the date of the investment;
  - (b) the name of each person or company through which the investment was made;
  - (c) a daily market valuation of the investment, any unrealized gain or loss of the investment and related supporting documentation;
  - (d) a description of each asset or instrument in which the investment was made;

- (e) the identity of each permitted depository where each asset, as applicable, or instrument is deposited;
- (f) the date on which the investment was liquidated or otherwise disposed of and the realized gain or loss;
- (g) the name of each person or company liquidating or disposing of the investment.

#### **Records of currency conversion – regulated clearing agency**

- 40.** A regulated clearing agency must keep a record of each conversion of customer collateral from one currency to another.

### **PART 7 REPORTING AND DISCLOSURE BY A REGULATED CLEARING AGENCY**

#### **Disclosure to direct intermediaries by regulated clearing agency**

- 41. (1)** Before receiving the first cleared derivative from, for or on behalf of a customer, a regulated clearing agency must provide written disclosure describing all of the following to the direct intermediary through which the derivative is cleared:
- (a) the rules, policies or procedures of the regulated clearing agency that govern the segregation and use of customer collateral and the transfer or liquidation of a cleared derivative of a customer in the event of a direct intermediary's default;
  - (b) the impact of laws, including bankruptcy and insolvency laws, on the customer, its positions and customer collateral in the event of a direct intermediary's default;
  - (c) the circumstances under which an interest or ownership rights in the customer collateral may be enforced by the regulated clearing agency, direct intermediary or the customer.
- (2)** After accepting the first cleared derivative from, for or on behalf of a customer, each time that the regulated clearing agency makes any change to the rules, policies or procedures referred to in paragraph (1)(a), the regulated clearing agency must provide written disclosure to the direct intermediary through which the derivative is cleared, within a reasonable period of time, describing the changes made to the rules, policies or procedures.

#### **Customer information – regulated clearing agency**

- 42.** A regulated clearing agency must have rules, policies or procedures reasonably designed to confirm that the information it receives from a direct intermediary in accordance with subsection 24(1) is complete and received in a timely manner.

### **Customer collateral report - regulatory**

43. A regulated clearing agency that receives customer collateral must electronically submit to the regulator or securities regulatory authority, within 10 business days of the end of each calendar month, a completed Form 94-102F3 *Customer Collateral Report: Regulated Clearing Agency*.

### **Customer collateral report – direct intermediary**

44. A regulated clearing agency that receives customer collateral must make available to each of its direct intermediaries a report, calculated and available on a daily basis, setting out all of the following:
- (a) the current value of the cleared derivative positions of each customer of the direct intermediary;
  - (b) the current value, asset type and quantity of customer collateral received from the direct intermediary for or on behalf of each customer of the direct intermediary that is held by the regulated clearing agency;
  - (c) the total current value of customer collateral received from the direct intermediary that is held at a permitted depository;
  - (d) the location of each permitted depository at which the customer collateral is held.

### **Disclosure of investment of customer collateral**

45. (1) Before receiving the first cleared derivative from, for or on behalf of a customer, a regulated clearing agency that invests customer collateral must disclose in writing its investment guidelines and policy to the direct intermediary through which the derivative is cleared.
- (2) A regulated clearing agency that invests customer collateral must promptly disclose in writing any change to its investment guidelines and policy to the direct intermediary through which the derivative is cleared.

## **PART 8 TRANSFER OF POSITIONS**

### **Transfer of customer collateral and positions**

46. (1) Subject to subsection (3), a regulated clearing agency and a defaulting direct intermediary must facilitate a transfer of customer positions and customer collateral or their liquidation proceeds from the defaulting direct intermediary to one or more non-defaulting direct intermediaries.
- (2) Subject to subsection (3), a regulated clearing agency and a non-defaulting direct intermediary must facilitate a transfer of the customer's positions and customer collateral

from the non-defaulting direct intermediary to one or more non-defaulting direct intermediaries.

- (3) Each of a regulated clearing agency and a direct intermediary may facilitate a transfer described in subsection (1) or (2) in respect of a customer only if all of the following apply:
- (a) the customer has requested or consented to the transfer;
  - (b) the customer's account is not currently in default;
  - (c) the transferred positions will have appropriate margin at the receiving direct intermediary;
  - (d) any remaining positions will have appropriate margin at the transferring direct intermediary;
  - (e) the receiving direct intermediary has consented to the transfer.

#### **Transfer from a clearing intermediary**

47. A clearing intermediary that provides clearing services for an indirect intermediary must have rules, policies or procedures in respect of the portability and transfer of customer positions and customer collateral in the event of a default by the clearing intermediary that include a credible mechanism for transferring the positions and customer collateral of the indirect intermediary's customers, upon a default by the indirect intermediary or at the request of the indirect intermediary's customer, to one or more non-defaulting clearing intermediaries.

### **PART 9 SUBSTITUTED COMPLIANCE**

48. (1) A clearing intermediary located in a foreign jurisdiction is deemed to satisfy the Parts and sections of this Instrument listed in Appendix A in respect of a cleared derivative entered into by, for or on behalf of a local customer if
- (a) the cleared derivative is cleared at a regulated clearing agency, and
  - (b) the clearing intermediary is all of the following:
    - (i) registered, licensed or otherwise permitted to perform the services of a clearing intermediary in the jurisdiction where its primary regulator is located;
    - (ii) in compliance with the requirements of the laws of a foreign jurisdiction as set out in Appendix A.

(2) A regulated clearing agency located in a foreign jurisdiction is deemed to satisfy the Parts and sections of this Instrument listed in Appendix A in respect of a cleared derivative entered into by, for or on behalf of a local customer if the regulated clearing agency is in compliance with all of the following:

- (a) the terms and conditions of any recognition or exemption decision made by a securities regulatory authority in respect of the regulated clearing agency;
- (b) the requirements of the laws of a foreign jurisdiction as set out in Appendix A.

## **PART 10 EXEMPTIONS**

49. (1) The regulator or the securities regulatory authority may grant an exemption to this Instrument, in whole or in part, subject to such conditions or restrictions as may be imposed in the exemption.
- (2) Despite subsection (1), in Ontario, only the regulator may grant an exemption.
- (3) Except in Alberta and Ontario, an exemption referred to in subsection (1) is granted under the statute referred to in Appendix B of National Instrument 14-101 *Definitions* opposite the name of the local jurisdiction.

## **PART 11 EFFECTIVE DATE**

### **Effective date**

50. This Instrument comes into force on [•].

## APPENDIX A

### **PART A EQUIVALENT REQUIREMENTS FOR PARTS AND SECTIONS RELATING TO CLEARING INTERMEDIARIES**

Further to section 48(1) of this Instrument, a clearing intermediary that satisfies the requirements of section 48(1) is deemed to satisfy the Parts and sections of this Instrument listed in the table below where the clearing intermediary is in compliance with the provisions of the laws of the foreign jurisdiction as set out opposite the Part or section of this Instrument.

Parts and sections of this Instrument applicable to a clearing intermediary	Compliance with foreign customer protection regime required to permit substituted compliance

### **PART B EQUIVALENT REQUIREMENTS FOR PARTS AND SECTIONS RELATING TO REGULATED CLEARING AGENCIES**

Further to section 48(2) of this Instrument, a regulated clearing agency that satisfies the requirements of section 48(2) is deemed to satisfy the Parts and sections of this Instrument listed in the table below where the regulated clearing agency is in compliance with the provisions of the laws of the foreign jurisdiction as set out opposite the Part or section of this Instrument.

Parts and sections of this Instrument applicable to a regulated clearing agency	Compliance with foreign customer protection regime required to permit substituted compliance

**PROPOSED NATIONAL INSTRUMENT 94-102**  
**DERIVATIVES: CUSTOMER CLEARING AND PROTECTION OF CUSTOMER COLLATERAL**  
**AND POSITIONS**

**FORM 94-102F1 CUSTOMER COLLATERAL REPORT: DIRECT INTERMEDIARY**

This Form 94-102F1 is to be completed by each direct intermediary in order to comply with its reporting obligations to the local securities regulator under subsection 25(1) of National Instrument 94-102 *Derivatives: Customer Clearing and Protection of Customer Collateral and Positions* (the “Instrument”).

Reporting Date	DD/MM/YY
Reporting Period <sup>1</sup>	DD/MM/YY – DD/MM/YY

Reporting direct intermediary
Name and LEI <sup>2</sup>

Table A is to be completed by each direct intermediary that receives customer collateral from a customer or from an indirect intermediary in accordance with the Instrument. In Section 1, complete a separate line for each customer that has posted customer collateral to the reporting direct intermediary. In Section 2, complete a separate line for each customer of an indirect intermediary for whom the indirect intermediary has posted customer collateral to the reporting direct intermediary. Where a LEI is not available please provide an Interim LEI or, if not available, the complete legal name of the customer.

**Table A**

A.	LEI of customer	Customer collateral			
		Total value of non-cash customer collateral posted to the direct intermediary as of the last business day of the Reporting Period	Total value of customer collateral posted to the direct intermediary as of the last business day of the Reporting Period	Maximum value of customer collateral posted to the direct intermediary during the Reporting Period	Average value of customer collateral posted to the direct intermediary over the Reporting Period
Section 1.	[Any customer that has posted customer collateral to the reporting direct intermediary]				

<sup>1</sup> The Reporting Period is the calendar month preceding the Reporting Date

<sup>2</sup> Where a LEI is not available, please provide an Interim LEI or, if not available, please provide the complete legal name of the reporting direct intermediary together with the complete address of its head office.

[National Instrument 94-102, Form 94-102F1  
*Customer Collateral Report: Direct Intermediary*]

Section 2.	[Any customer for whom an indirect intermediary has posted customer collateral to the reporting direct intermediary]				
<u>Aggregate total</u>					

Table B is to be completed by each direct intermediary that receives customer collateral from a customer or from a clearing intermediary in accordance with the Instrument. Complete a separate line for each location at which customer collateral is held by or for the reporting direct intermediary. Where a LEI is not available, please provide an Interim LEI or, if not available, the complete legal and operating name(s) of the permitted depository.

**Table B**

B.	LEI of permitted depository or reporting direct intermediary	Customer collateral			
		Total value of non-cash customer collateral held by or for the direct intermediary as of the last business day of the Reporting Period	Total value of customer collateral held by or for the direct intermediary as of the last business day of the Reporting Period	Maximum value of customer collateral held by or for the direct intermediary during the Reporting Period	Average value of customer collateral held by or for the direct intermediary over the Reporting Period
1.	[Reporting direct intermediary, if holding customer collateral itself]				
2.	[Any permitted depository holding customer collateral for the reporting direct intermediary]				
<u>Aggregate total</u>					

Table C is to be completed by each direct intermediary that has deposited customer collateral with a regulated clearing agency in accordance with the Instrument. Complete a separate line for each regulated clearing agency with which the reporting direct intermediary has deposited customer collateral. Where a LEI is not available, please provide an Interim LEI or, if not available, the complete legal and operating name(s) of the regulated clearing agency.

**Table C**

C.	LEI of regulated clearing agency	Customer collateral			
		Total value of non-cash customer collateral deposited with a regulated clearing agency as of the last business day of the Reporting Period	Total value of customer collateral deposited with a regulated clearing agency as of the last business day of the Reporting Period	Maximum value of customer collateral deposited with a regulated clearing agency during the Reporting Period	Average value of customer collateral deposited with a regulated clearing agency over the Reporting Period
1.	[Any regulated clearing agency with which the reporting direct intermediary has deposited customer collateral]				
<u>Aggregate total:</u>					

**PROPOSED NATIONAL INSTRUMENT 94-102**  
**DERIVATIVES: CUSTOMER CLEARING AND PROTECTION OF CUSTOMER COLLATERAL**  
**AND POSITIONS**

**FORM 94-102F2 CUSTOMER COLLATERAL REPORT: INDIRECT INTERMEDIARY**

This Form 94-102F2 is to be completed by each person or company that acts as an indirect intermediary in order to comply with its reporting obligations to the local securities regulator under subsection 25(2) of National Instrument 94-102 *Derivatives: Customer Clearing and Protection of Customer Collateral and Positions* (the “Instrument”).

Reporting Date	DD/MM/YY
Reporting Period <sup>1</sup>	DD/MM/YY – DD/MM/YY

Reporting indirect intermediary
Name and LEI <sup>2</sup>

Table A is to be completed by each indirect intermediary that receives customer collateral from a customer in accordance with the Instrument. Complete a separate line for each customer that has posted customer collateral to the reporting indirect intermediary. Where a LEI is not available, please provide an Interim LEI or, if not available, the complete legal name of the customer.

**Table A**

A.	LEI of customer	Customer collateral			
		Total value of non-cash customer collateral posted to the indirect intermediary as of the last business day of the Reporting Period	Total value of customer collateral posted to the indirect intermediary as of the last business day of the Reporting Period	Maximum value of customer collateral posted to the indirect intermediary during the Reporting Period	Average value of customer collateral posted to the indirect intermediary over the Reporting Period
1.	[Any customer that has posted customer collateral to the reporting indirect intermediary]				
<u>Aggregate total</u>					

<sup>1</sup> The Reporting Period is the calendar month preceding the Reporting Date.

<sup>2</sup> Where a LEI is not available, please provide an Interim LEI or, if not available, please provide the complete legal name of the reporting indirect intermediary together with the complete address of its head office.

Table B is to be completed by each indirect intermediary that receives customer collateral from a customer in accordance with the Instrument. Complete a separate line for each location at which customer collateral is held by or for the reporting indirect intermediary. Where a LEI is not available, please provide an Interim LEI or, if not available, the complete legal and operating name(s) of the permitted depository.

**Table B**

B.	LEI of permitted depository or reporting indirect intermediary	Customer collateral			
		Total value of non-cash customer collateral held by or for the indirect intermediary as of the last business day of the Reporting Period	Total value of customer collateral held by or for the indirect intermediary as of the last business day of the Reporting Period	Maximum value of customer collateral held by or for the indirect intermediary during the Reporting Period	Average value of customer collateral held by or for the indirect intermediary over the Reporting Period
1.	[Reporting indirect intermediary, if holding customer collateral itself]				
2.	[Any permitted depository holding customer collateral for the reporting indirect intermediary]				
<u>Aggregate total:</u>					

Table C is to be completed by each indirect intermediary that has posted customer collateral to a direct intermediary in accordance with the Instrument. Complete a separate line for each direct intermediary with which the reporting indirect intermediary has deposited customer collateral. Where a LEI is not available, please provide an Interim LEI or, if not available, the complete legal and operating name(s) of the direct intermediary.

**Table C**

C.	LEI of direct intermediary	Customer collateral			
		Total value of non-cash customer collateral posted to a direct intermediary as of the last business day of the Reporting Period	Total value of customer collateral posted to a direct intermediary as of the last business day of the Reporting Period	Maximum value of customer collateral posted to a direct intermediary during the Reporting Period	Average value of customer collateral posted to a direct intermediary over the Reporting Period
1.	[Any direct intermediary with which the reporting indirect intermediary has posted customer collateral]				
<u>Aggregate total:</u>					

**PROPOSED NATIONAL INSTRUMENT 94-102**  
**DERIVATIVES: CUSTOMER CLEARING AND PROTECTION OF CUSTOMER COLLATERAL**  
**AND POSITIONS**

**FORM 94-102F3 CUSTOMER COLLATERAL REPORT: REGULATED CLEARING AGENCY**

This Form 94-102F3 is to be completed by each regulated clearing agency in order to comply with its reporting obligations to the local securities regulator under section 43 of National Instrument 94-102 *Derivatives: Customer Clearing and Protection of Customer Collateral and Positions* (the “Instrument”).

Reporting Date	DD/MM/YY
Reporting Period <sup>1</sup>	DD/MM/YY – DD/MM/YY

Reporting regulated clearing agency
Name and LEI <sup>2</sup>

Table A is to be completed by each regulated clearing agency that receives customer collateral from a direct intermediary in accordance with the Instrument. Complete a separate line for each direct intermediary that has posted customer collateral with the reporting regulated clearing agency. Where a LEI is not available please provide an Interim LEI or, if not available, the complete legal name of the direct intermediary.

**Table A**

A.	LEI of direct intermediary	Customer collateral			
		Total value of non-cash customer collateral posted to the regulated clearing agency as of the last business day of the Reporting Period	Total value of customer collateral posted to the regulated clearing agency as of the last business day of the Reporting Period	Maximum value of customer collateral posted to the regulated clearing agency during the Reporting Period	Average value of customer collateral posted to the regulated clearing agency over the Reporting Period
1.	[Any direct intermediary that has posted customer collateral with the reporting regulated clearing agency]				
<u>Aggregate total:</u>					

<sup>1</sup> The Reporting Period is the calendar month preceding the Reporting Date.

<sup>2</sup> Where a LEI is not available, please provide an Interim LEI or, if not available, please provide the complete legal name of the reporting regulated clearing agency together with the complete address of its head office.

Table B is to be completed by each regulated clearing agency that holds customer collateral in accordance with the Instrument. Complete a separate line for each location at which customer collateral is held by or for the reporting regulated clearing agency. Where a LEI is not available please provide an Interim LEI or, if not available, the complete legal and operating name(s) of the permitted depository.

**Table B**

B.	LEI of permitted depository or reporting regulated clearing agency	Customer collateral			
		Total value of non-cash customer collateral held by or for the regulated clearing agency as of the last business day of the Reporting Period	Total value of customer collateral held by or for the regulated clearing agency as of the last business day of the Reporting Period	Maximum value of customer collateral held by or for the regulated clearing agency during the Reporting Period	Average value of customer collateral held by or for the regulated clearing agency over the Reporting Period
1.	[Reporting regulated clearing agency, if holding customer collateral itself]				
2.	[Any permitted depository holding customer collateral for the reporting regulated clearing agency]				
<u>Aggregate total</u>					

**ANNEX C**

**COMPANION POLICY 94-102CP**

***DERIVATIVES: CUSTOMER CLEARING AND PROTECTION OF CUSTOMER COLLATERAL AND POSITIONS***

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## **PART 1 GENERAL COMMENTS**

### **Introduction**

This Companion Policy (“CP”) sets out the views of the Canadian Securities Administrators (the “CSA” or “we”) on various matters relating to National Instrument 94-102 *Derivatives: Customer Clearing and Protection of Customer Collateral and Positions* (the “Instrument”) and related securities legislation.

Other than this Part, the numbering of Parts, sections, subsections, paragraphs and subparagraphs in this CP generally corresponds to the numbering in the Instrument. Any general guidance for a Part appears immediately after the Part’s name. Any specific guidance on a section, subsection, paragraph or subparagraph in the Instrument follows any general guidance. If there is no guidance for a Part, section, subsection paragraph or subparagraph, the numbering in this CP will skip to the next provision that does have guidance.

Unless otherwise stated, any reference to a Part, section, subsection, paragraph, subparagraph or definition in this CP is a reference to the corresponding Part, section, subsection, paragraph, subparagraph or definition in the Instrument.

### **Definitions and interpretation**

Unless defined in the Instrument, terms used in the Instrument and in this CP have the meaning given to them in securities legislation including, National Instrument 14-101 *Definitions*.

### **Interpretation of terms used in the Instrument and in this CP**

A number of key terms are used in the Instrument and this CP, including the terms that follow.

- “Clearing services” refers to acts in furtherance of the clearing of a customer transaction. This includes, among other things: submitting customer transactions and associated collateral to a regulated clearing agency for clearing; monitoring and maintaining collateral requirements from the regulated clearing agency on behalf of a customer, including those for initial and variation margin; monitoring and maintaining excess collateral; recording and monitoring cleared positions, collateral received and valuations of both; and monitoring credit and liquidity limits.

Clearing services also include services provided from one clearing intermediary to another in furtherance of a customer transaction. For example, a direct intermediary would be providing clearing services to an indirect intermediary where it accepts a customer transaction that was originally submitted by a customer to the indirect intermediary and submits it to a regulated clearing agency.

- The term “lien” refers to a creditor’s claim against property to secure repayment of a debt.
- The term “position” refers to the aggregate amount of a derivative cleared by a regulated clearing agency for a customer at a point in time.
- “PFMI Report” means the April 2012 final report entitled *Principles for financial market infrastructures* published by the Bank for International Settlements’ Committee on Payments and Market Infrastructure (formerly the Committee on Payment and Settlement Systems) and the Technical Committee of the International Organization of Securities Commissions, as amended from time to time.

## Interpretation of terms defined in the Instrument

1. A “cleared derivative” is submitted to and cleared by a clearing agency, either voluntarily or in accordance with the clearing requirement set out in Proposed National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives*. The terms “directly” and “indirectly” refer to the chain of clearing intermediaries involved in a transaction. Where a customer interacts directly with a direct intermediary, the transaction would be considered to be directly submitted to and cleared by a clearing agency. Where an indirect intermediary submits a transaction to a direct intermediary for clearing on behalf of a customer, the transaction is considered to be indirectly submitted to the clearing agency.

A direct intermediary is not a customer where it transacts with a clearing agency of which it is a participant. However, a person or company that acts as a direct intermediary can be a customer when clearing its own proprietary transactions through another direct intermediary of a clearing agency where it is not itself a participant. An indirect intermediary is considered a clearing intermediary rather than a customer in a transaction where it is providing clearing services to a customer. However, a person or company acting as an indirect intermediary can be a customer to the extent that it is clearing its own proprietary transaction through another clearing intermediary. For certainty, there is always one and only one customer per clearing chain. The customer is the person or company entering into the transaction on its own behalf and accessing clearing services through one or more clearing intermediaries.

In a clearing chain that involves an indirect intermediary providing clearing services to a person or company, that person or company would be considered a customer of each clearing intermediary in the chain as well as of the regulated clearing agency. For example, where a customer submits a transaction to an indirect intermediary, it would be a customer of both the indirect intermediary and the direct intermediary that submits the transaction to the regulated clearing agency, as well as of the regulated clearing agency. If there were multiple indirect intermediaries involved in a transaction, the person or company would be considered a customer of each of these intermediaries.

We expect that, subject to any available exemption, a clearing intermediary offering clearing services to a customer must register as a derivatives dealer when such requirement is in place. CSA Consultation Paper 91-407 *Derivatives: Registration* (“Consultation Paper 91-407”) outlines the recommended business trigger for determining whether a person is in the business of trading derivatives.<sup>1</sup> These factors include intermediating transactions and providing clearing services to third-parties. Please refer to Consultation Paper 91-407 for further details.

With respect to “customer collateral”, we wish to point out that although a customer may deliver certain collateral to a clearing intermediary, this specific collateral may not be the collateral delivered to the regulated clearing agency to satisfy the customer’s margin requirements at the regulated clearing agency. A clearing intermediary may “upgrade” or “transform” the collateral delivered by the customer pursuant to their agreement. For example, a customer may deliver cash as collateral and, pursuant to their agreement, the clearing intermediary may deliver securities of an equivalent value to the regulated clearing agency. Any collateral, transformed, upgraded or otherwise, delivered to the regulated clearing agency on behalf of a customer would be considered customer collateral. Generally, the original collateral delivered by the customer is no longer considered customer collateral once it has been transformed or upgraded and therefore is no longer subject to the requirements of the Instrument. The transformed or upgraded collateral exchanged for the customer’s original collateral becomes the customer collateral that is subject to the Instrument and must be treated as customer collateral regardless of the number or type of transformations or upgrades it undergoes.

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<sup>1</sup> See subsection 6.1(b) of Consultation Paper 91-407.

Paragraph (b) of the definition of “customer collateral” refers to a situation where a clearing intermediary submits its own property to satisfy the obligations of one or more customers to the regulated clearing agency. An example of this would be a direct intermediary providing its own property to meet an inter-day margin call by the regulated clearing agency. Where a clearing intermediary submits its own property on behalf of a customer, this property must be treated as customer collateral.

A “direct intermediary” is a participant of the regulated clearing agency where a customer transaction is submitted for clearing. A direct intermediary is responsible for submitting a customer’s transaction to the regulated clearing agency and has obligations to the regulated clearing agency with respect to the transaction.

An “indirect intermediary” is a person or company that is not a participant of the regulated clearing agency where a transaction is submitted but that facilitates clearing on behalf of a customer. In order to clear its customer’s transaction, the indirect intermediary would enter into an agreement with a direct intermediary (or another indirect intermediary that would in turn submit the transaction to a direct intermediary) that would submit the transaction to the regulated clearing agency to be cleared. This clearing relationship is often referred to as “indirect customer clearing”. It is possible that a person or company that is a direct intermediary at one regulated clearing agency could also act as an indirect intermediary in order to access another regulated clearing agency, of which it is not a participant. The classification as a direct intermediary or indirect intermediary is not exclusive. A clearing intermediary can be a direct intermediary for some transactions and an indirect intermediary for others. A person or company providing services in respect of a cleared derivative would be considered a clearing intermediary for the purposes of the Instrument if it requires, receives or holds collateral from, for or on behalf of a customer. Accordingly, an intermediary that does not receive, hold or transfer collateral from, for on behalf of a customer would not be subject to the requirements under the Instrument even if it facilitates some limited aspects of the relationship between a clearing intermediary and a customer with respect to cleared derivatives (e.g., organizing orders for derivatives).

The term “initial margin” refers to collateral required by a regulated clearing agency to cover potential future losses resulting from expected changes in the value of a cleared derivative over a pre-determined close-out period with a certain level of confidence.

The term “participant” refers to a clearing intermediary that is a member of a regulated clearing agency.

A “permitted depository” is a person or company acceptable for holding customer collateral posted with a clearing intermediary or regulated clearing agency. A clearing intermediary that itself meets the requirements of the definition may hold customer collateral directly and is not required to use a third-party permitted depository.

In recognition of the international nature of the derivatives market, paragraph (c) of the definition permits foreign banks or trust companies to act as permitted depositories and hold customer collateral, provided they are regulated as a bank or trust company in a permitted jurisdiction. Subparagraph (d)(ii) of the definition also permits a prudentially regulated foreign entity other than a bank or trust company to act as a permitted depository for customer collateral, provided that it is registered, licensed or otherwise permitted to perform the services of a clearing intermediary in a permitted jurisdiction.

The term “permitted investment” sets out a principles-based approach to determining the types of instruments in which a clearing intermediary or regulated clearing agency may invest customer collateral, in accordance with the provisions of the Instrument. The term is intended to cover an investment in an instrument that is secured by, or is a claim on, high-quality obligors, and which allows for quick liquidation with little, if any, adverse price effect, for the purpose of mitigating market, credit and liquidity risk.

We are of the view that a clearing intermediary or regulated clearing agency that invests customer collateral in accordance with the Instrument should ensure such investment is:

- consistent with its overall risk-management strategy,
- fully disclosed to its customers,
- limited to instruments that are secured by, or are claims on, high-quality obligors, and
- can be liquidated quickly with little, if any, adverse price effect.

We are also of the view that a clearing intermediary or regulated clearing agency should not invest customer collateral in its own securities or those of its affiliated entities. Examples of instruments that would be considered permitted investments by the local securities regulatory authority include each of the following:

- debt securities issued by or guaranteed by the Government of Canada or the government of a province or territory of Canada;
- debt securities that are issued or guaranteed by a municipal corporation in Canada;
- certificates of deposit, that are not securities, issued by a bank listed in Schedule I, II or III to the Bank Act (Canada) (“Bank Act”);
- commercial paper fully guaranteed as to principal and interest by the Government of Canada;
- interests in money market mutual funds.

We are also of the view that foreign investments in high-quality obligors exhibiting the same conservative characteristics as the instruments listed above would also be acceptable.

Paragraph (a) of the definition of “permitted jurisdiction” captures jurisdictions where the primary regulators of foreign banks authorized under the Bank Act to carry on business in Canada, subject to supervision by the Office of the Superintendent of Financial Institutions (“OSFI”), are located. The following countries and their political subdivisions are included: Belgium, France, Germany, Ireland, Japan, Netherlands, Singapore, Switzerland, United Kingdom (including Scotland) and the United States of America.

For Paragraph (b) of the definition of “permitted jurisdiction,” in the case of the euro, where the currency does not have a single “country of origin”, the provision will be read to include all countries in the euro area<sup>2</sup> and countries using the euro under a monetary agreement with the European Union.<sup>3</sup>

The definition of “qualifying central counterparty” is based on the qualifying central counterparty standard set out in the July 2012 final report entitled *Capital requirements for bank exposures to central counterparties*<sup>4</sup> published by the Basel Committee on Banking Supervision (“BCBS”). The BCBS has further stated<sup>5</sup> that if a regulator of a central counterparty has provided a public statement that the central counterparty has the status of a qualifying central counterparty, then the central counterparty may be considered to be a qualifying central counterparty. We

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<sup>2</sup> European Union, Economic and Financial Affairs, *What is the euro area?*, May 18, 2015, online: European Union ([http://ec.europa.eu/economy\\_finance/euro/adoption/euro\\_area/index\\_en.htm](http://ec.europa.eu/economy_finance/euro/adoption/euro_area/index_en.htm)).

<sup>3</sup> European Union, Economic and Financial Affairs, *The euro outside the euro area*, April 9, 2014, online: European Union ([http://ec.europa.eu/economy\\_finance/euro/world/outside\\_euro\\_area/index\\_en.htm](http://ec.europa.eu/economy_finance/euro/world/outside_euro_area/index_en.htm)).

<sup>4</sup> Basel Committee on Banking Supervision (BCBS), *Capital requirements for bank exposures to central counterparties*, July 2012, online: Bank for International Settlements (<http://www.bis.org>).

<sup>5</sup> BCBS, *Basel III counterparty credit risk and exposures to central counterparties – Frequently asked questions*, updated December 2012, online: Bank for International Settlements (<http://www.bis.org>).

are similarly of the view that a local counterparty may rely on a public statement by a regulator of a central counterparty that the central counterparty is a qualifying central counterparty. The qualifying central counterparty standard is also discussed in CSA Multilateral Staff Notice 24-311 *Qualifying Central Counterparties*.

While the term “segregate” means to separately hold or account for customer collateral, consistent with the PFMI Report, accounting segregation is acceptable.

### **Application**

2. The Instrument applies to a clearing intermediary or foreign regulated clearing agency that provides clearing services to a local customer, but only in respect of a local customer’s cleared derivatives. For example, a clearing intermediary providing clearing services to a local customer would be subject to the requirements of the Instrument only as they relate to the local customer and the cleared derivatives of the local customer. The Instrument is not applicable to the clearing intermediary when providing clearing services to foreign customers. The Instrument has broader application with respect to a regulated clearing agency located in a local jurisdiction; such a regulated clearing agency is subject to the requirements of the Instrument in respect of the cleared derivatives of all of its customers (whether they are local customers or not).

## **PART 2 TREATMENT OF CUSTOMER COLLATERAL BY A CLEARING INTERMEDIARY**

Part 2 contains requirements for the treatment of customer collateral by a clearing intermediary.

### **Segregation of customer collateral – clearing intermediary**

3. (1) Subsection 3(1) requires a clearing intermediary to segregate customer collateral from its own property, including from collateral advanced for a proprietary position. For example, a direct intermediary’s proprietary positions (i.e., a house account) would be required to be held or accounted for separately from customer positions. Similarly, an indirect intermediary would be required to establish a separate account for its customers with its direct intermediary, so that the indirect intermediary’s proprietary positions are held or accounted for separately from those of its customers. Records maintained by a clearing intermediary must make it clear that customer accounts are for the benefit of customers only.

Recognizing that methods for segregating customer collateral at the clearing intermediary level may differ depending on collateral and entity type, we are of the view that parties should have the benefit of flexibility in their collateral arrangements. However, the principle remains that notwithstanding the legal arrangement under which customer collateral is posted with a clearing intermediary, the clearing intermediary must treat customer collateral posted with it as belonging to customers. For example, in a title transfer collateral arrangement, where the title to the property posted as collateral is transferred to the person or company collecting the collateral, despite any such transfer of legal title from the customer to a clearing intermediary, such clearing intermediary must treat any property transferred as collateral by or on behalf of a customer and relating to that customer’s cleared derivatives as customer collateral and as the property of that customer.

### **Holding of customer collateral – clearing intermediary**

4. We are of the view that a clearing intermediary that holds customer collateral at a permitted depository in accordance with the Instrument should take reasonable commercial efforts to confirm that the permitted depository:

- qualifies as a permitted depository under the Instrument;

- has appropriate rules, policies and procedures, including robust accounting practices, to help ensure the integrity of the customer collateral and minimize and manage the risks associated with the safekeeping and transfer of the collateral;
- maintains securities in an immobilised or dematerialised form for their transfer by book entry;
- protects customer collateral against custody risk through appropriate rules and procedures consistent with its legal framework;
- employs a robust system that ensures segregation between the permitted depository's own property and the property of its participants and segregation among the property of participants, and where supported by the legal framework, supports operationally the segregation of property belonging to a participant's customers on the participant's books and facilitates the transfer of customer collateral;
- identifies, measures, monitors, and manages its risks from other activities that it may perform;
- facilitates prompt access to customer collateral, when required.

If a clearing intermediary meets the requirements set out in the definition of a permitted depository, it may hold collateral itself and is not required to hold such customer collateral at a third party depository. For example, a Canadian financial institution that acts as a clearing intermediary would be permitted to hold customer cash or securities provided it did so in accordance with the requirements of the Instrument.

The customer collateral of multiple customers may be commingled in an omnibus customer account. However, the record-keeping obligations in the Instrument require the clearing intermediary to identify the positions and collateral held for each individual customer within an omnibus customer account. Where a clearing intermediary deposits customer collateral with a permitted depository, the clearing intermediary is responsible for ensuring the permitted depository maintains appropriate books and records to ensure customer collateral can be attributed to each customer.

#### **Excess margin – clearing intermediary**

5. We would interpret the requirement that a clearing intermediary identify and record the excess margin that it holds as only applying to that excess margin. For example, a direct intermediary would not be required to keep records of the excess margin required from a customer by an indirect intermediary to which it provides clearing services.

#### **Use of customer collateral – clearing intermediary**

6. (2) The use of customer collateral attributable to one customer to satisfy the obligations of another customer is not permitted. Although customer collateral may be held in one omnibus account, such collateral is not available to satisfy customer obligations generally. Therefore, a clearing model that allows recourse to a non-defaulting customer's collateral, including any model that permits fellow customer risk, violates this provision and would not be permitted to be offered to customers. For certainty, fellow customer risk is found in a clearing model that allows the customer collateral of a non-defaulting customer to be used to settle the obligations of a defaulting customer. The pooling of customer collateral held by a clearing intermediary pursuant to applicable bankruptcy and insolvency laws would not be considered a use of customer collateral by the clearing intermediary and is permitted where required by applicable laws.

(3) Subsection 6(3) recognizes that certain clearing arrangements involve the granting of security interests in customer collateral. Should an improper lien be imposed on customer collateral, the clearing intermediary must

take all commercially reasonable steps to promptly address the improper lien. However, a lien over excess collateral is not restricted where the lien is imposed to secure or extend credit to the customer.

### **Investment of customer collateral – clearing intermediary**

7. (3) Although losses in the value of invested customer collateral are not to be allocated to a customer, we are of the view that parties should be free to contract for the allocation of gains resulting from a clearing intermediary's investment activities in accordance with the Instrument. Subsection 7(3) provides that any loss resulting from a permitted investment of customer collateral must be borne by the investing clearing intermediary and not by a customer. This requirement relates only to investments made by a clearing intermediary using customer collateral, not to collateral provided by a customer. If, for example, a customer provided government bonds as collateral, and those bonds lost market value, the clearing intermediary would not be required to bear those losses. Similarly, where a customer provided collateral to a clearing intermediary and it was transformed into government bonds to be used as customer collateral posted to a regulated clearing agency, the clearing intermediary would not be required to bear any loss in market value of the transformed customer collateral.

### **Use of customer collateral – indirect intermediary default**

8. An example of when a clearing intermediary may apply customer collateral to settle the obligations of a defaulting indirect intermediary is when a customer's default causes the default of the indirect intermediary. In such case, a direct intermediary could use the defaulting customer's collateral to satisfy the indirect intermediary's obligations attributable to the customer's default.

### **Acting as a clearing intermediary**

9. (1) Paragraph 9(1)(a) applies to clearing intermediaries located in Canada. Prudential regulation by an appropriate regulatory authority in Canada should ensure that a clearing intermediary is adequately capitalized and has sufficient liquidity such that it is financially sound and does not present a significant solvency risk to customers. In Canada, prudential regulation of federally regulated financial institutions is undertaken by OSFI. Other regulators that perform prudential oversight include the Investment Industry Regulatory Organization of Canada ("IIROC") and certain provincial prudential market regulators, such as the Autorité des marchés financiers in Québec, or other local securities regulatory authorities when the proposed registration regime for over-the-counter derivatives ("OTC derivatives") is implemented.

Paragraph 9(1)(b) applies to clearing intermediaries located in a foreign jurisdiction. In order to provide clearing services to a local customer, such clearing intermediaries must be registered, licensed or otherwise permitted to perform the services of a clearing intermediary in a permitted jurisdiction and must do so in accordance with the laws and regulations of that permitted jurisdiction. This would include, for example, a Commodity Futures Trading Commission ("CFTC") registered futures commission merchant authorized to provide clearing services for OTC derivatives by the CFTC.

The CSA Derivatives Committee is developing a registration regime that will apply to clearing intermediaries. Once in force, subject to any available exemptions, registration will be required for clearing intermediaries to offer clearing services to local customers.

(2) For greater certainty, pursuant to the application provisions of subsection 2, the requirement for a clearing intermediary to clear all transactions through a regulated clearing agency only applies to transactions with local customers.

### **Risk management – clearing intermediary**

**10.** Rules, policies and procedures designed to identify, monitor and manage material risks arising from offering clearing services to an indirect intermediary and management of a default by an indirect intermediary should include all of the following:

- following industry standard best practices for understanding an indirect intermediary's: (i) identity and corporate structure, (ii) financial resources (e.g., by establishing credit and liquidity limits), (iii) product knowledge (e.g., by establishing a list of the indirect intermediary's products allowed to be cleared) and (iv) technical infrastructure (e.g., establishing adequate operational capacity and communication links between the indirect intermediary and the clearing intermediary);
- measuring and monitoring the positions of each indirect intermediary including: (i) the daily valuation of the indirect intermediary's positions and cash flow obligations and (ii) market risk resulting from those positions;
- a default management plan which describes the steps followed in the event of an indirect intermediary's default.

### **Risk management – indirect intermediary**

**11.** Rules, policies and procedures designed to identify, monitor and manage material risks arising from offering indirect clearing services to customers should include all of the following:

- following industry standard best practices for understanding a customer's: (i) identity and corporate structure, (ii) financial resources (e.g., by establishing credit and liquidity limits), (iii) product knowledge (e.g., by establishing a list of the indirect intermediary's products allowed to be cleared) and (iv) technical infrastructure (e.g., establishing adequate operational capacity and communication links between the indirect intermediary and the customer);
- measuring and monitoring the positions of each customer including (i) the daily valuation of the customer's positions and cash flow obligations and (ii) market risk resulting from those positions.

## **PART 3 RECORD-KEEPING BY A CLEARING INTERMEDIARY**

Part 3 outlines the minimum record-keeping requirements that apply to clearing intermediaries. The effectiveness of the customer protections required under the Instrument is predicated on accurate and thorough record-keeping by clearing intermediaries.

### **Retention of records – clearing intermediary**

**12.** The records required to be prepared pursuant to this Part and Part 4 must be retained for at least 7 years and in accordance with record-retention practice in Canada and the timing requirements under the limitations acts in each local jurisdiction. Records prepared in relation to a cleared derivative include any customer profiles or other information collected from a customer prior to the date upon which a transaction for the customer is entered into and must be kept for at least 7 years after the date upon which a customer's last cleared derivative expires or terminates.

### **Books and records – clearing intermediary**

**13. (3)** The description of customer collateral in respect of paragraph 13(3)(b) should include an industry standard security identifier such as a CUSIP or ISIN code or, if an identifier is not available, a plain language description of the collateral.

We are of the view that accurate record-keeping requires, at minimum, daily valuations of customer collateral using industry standard best practice methodologies. With respect to records required to be kept under paragraph 13(3)(c):

- subparagraph (i) refers to any revenue generated by the customer collateral, including, for example, dividend pay-outs relating to securities and coupon payments relating to debt instruments;
- subparagraph (ii) refers to any changes in the value of property forming part of the customer collateral, including, for example, an increase or decrease in the value of a security;
- subparagraph (iii) refers to charges that have accrued, or may accrue, against the customer and have been agreed to between the clearing intermediary and the customer; such charges may include, for example, transaction or currency exchange charges, or charges relating to the settlement or termination of a cleared derivative.

### **Separate records – multiple clearing intermediaries**

**18.** Where a clearing intermediary allows a person or company to act as an indirect intermediary, the clearing intermediary assumes record-keeping obligations relating to the indirect intermediary and its customers. The effect of paragraphs 18(a) and (b) together is to enable the indirect intermediary to easily identify its own positions and property, and the positions and collateral held for, or on behalf, of each customer.

### **Records of investment of customer collateral – clearing intermediary**

**19.** We are of the view that the requirement in subsection 19(d) would be fulfilled by providing a unique identifier from an industry-accepted identifying standard, such as an ISIN or CUSIP number or, if an identifier is not available, a plain language description of each instrument or asset.

### **Records of currency conversion – clearing intermediary**

**20.** We are of the view that currency conversion trade records should include, at minimum, all of the following:

- the identity of the customer as represented by its legal entity identifier (“LEI”) or the name or other identifier of the customer where the customer is ineligible for a LEI;
- the date of the currency exchange;
- the amount and original currency of the funds to be exchanged;
- the exchange rate at which the currency exchange is made;
- the amount and new currency resulting from the exchange;
- the name of the institution which made the exchange and/or provided the exchange rate.

## **PART 4**

### **REPORTING AND DISCLOSURE BY A CLEARING INTERMEDIARY**

Part 4 outlines certain disclosure and reporting required to be made by a clearing intermediary to customers, regulated clearing agencies and the local securities regulatory authority. Disclosure required to be provided to customers under this Part is not required on a transaction by transaction basis.

The written disclosure required under sections 21, 22, 23 and 27 is necessary only once upon the opening of each customer account, not prior to each cleared derivative transaction. The disclosure and notice of changes to the disclosure can be provided in electronic form by delivering copies of required materials or providing links to online information. Disclosures can be incorporated into legal agreements between parties. Where there are multiple clearing intermediaries, direct intermediaries and indirect intermediaries may provide disclosure either to a clearing intermediary closer in the transaction chain to the customer or directly to the customer. Written disclosure can be provided in electronic form by delivering copies of required materials or by providing links to online information to the customer or clearing intermediary.

Where clearing intermediaries are already engaged in transactions relating to cleared derivatives with regulated clearing agencies, other clearing intermediaries or customers before the Instrument comes into force, the written disclosure required to be delivered under this Part must be delivered before receiving or submitting the first cleared derivative after the Instrument comes into force.

We acknowledge the confidential nature of the information reported to the local securities regulatory authority, and each local securities regulatory authority will treat it as such, subject to applicable legislation adopted by each province and territory, including any applicable freedom of information and protection of privacy legislation. However, information may be shared with self-regulatory organizations or other relevant regulatory authorities.

#### **Clearing intermediary delivery of disclosure by regulated clearing agency**

**21.** Section 21 requires a clearing intermediary to provide disclosure, including investment guidelines and policies for investing customer collateral, received from a regulated clearing agency pursuant to sections 41 and 45 to its customer. Where there is a chain of clearing intermediaries, the direct intermediary may provide this disclosure to the indirect intermediary, which is then required to provide this disclosure to the customer. Both subsections 41(2) and 45(2) require a regulated clearing agency to disclose any changes to the information previously disclosed. A clearing intermediary is required to promptly send to its customers all of the information related to changes in the disclosure provided by a regulated clearing agency under sections 41 and 45.

#### **Disclosure to customer by clearing intermediary**

**22.** Customer collateral held at the clearing intermediary level may receive different treatment from customer collateral held at the regulated clearing agency in the event of a clearing intermediary's bankruptcy or insolvency. The disclosure required by this provision should provide customers with clear information on the treatment of their collateral in a default situation. For example, there may be situations where customer collateral held in a customer account maintained by a clearing intermediary would be combined with the property of other customers with uncleared derivatives.

The information given in the written disclosure should assist customers in evaluating: (i) the level of protection provided, (ii) the manner in which segregation and the transfer of assets is achieved (including the method for determining the value at which customer positions will be transferred) and (iii) any risks or uncertainties associated with such arrangements. Disclosure helps customers assess the related risks and conduct due diligence when entering into transactions that are cleared at the regulated clearing agency through one or more clearing intermediaries.

Examples of the information that the disclosure should provide include all of the following:

- which bankruptcy and insolvency laws apply and how they may impact the clearing intermediary's ability in relation to its regulated clearing agency, clearing intermediaries and customers, to expeditiously terminate such relationships, transfer customer collateral, and enforce rights in relation to customer collateral;
- the process for recovering or transferring customer collateral should the clearing intermediary default;
- analysis of applicable laws governing clearing intermediaries;
- how the applicable legal framework protects customer collateral and any risks associated with that framework;
- where a customer is required to take proactive steps to protect its collateral, information on what steps a customer can take to do so, e.g., filing financing statements under laws regulating the creation and registration of security interests in personal property such as the *Personal Property Security Act* (Ontario) or such similar legislation in the local jurisdiction;
- the interaction of domestic and foreign laws applicable to customer collateral held by the clearing intermediary.

#### **Disclosure to customer by indirect intermediary**

**23.** The indirect intermediary should disclose to a customer any information relating to additional risks to customer positions and customer collateral that arise as a result of the indirect clearing relationship.

#### **Customer information – clearing intermediary**

**24.** In order to facilitate a timely transfer of collateral and positions in a default scenario, a regulated clearing agency should have sufficient information to identify each customer of a clearing intermediary, and each customer's positions and customer collateral. This identifying information must be submitted by the direct intermediary to each relevant regulated clearing agency, and must include the LEI, where the customer is eligible to be assigned a LEI in accordance with standards set by the Global Legal Entity Identifier System, or the name or other identifier of the customer.

#### **Customer collateral report - regulatory**

**25.** We are of the view that regular reporting on customer collateral deposits and holdings will assist the provincial securities regulatory authorities in monitoring customer collateral arrangements and developing and implementing rules to protect customer assets that are responsive to market practices. To that end, subsections 25(1) and 25(2) set out reporting requirements for direct intermediaries and indirect intermediaries, respectively, regarding customer collateral. A completed Form 94-102F1 or Form 94-102F2, as applicable, will provide the local securities regulatory authority with a snapshot of the value of collateral held by or deposited by each reporting clearing intermediary.

#### **Customer collateral report – customer**

**26.** The customer collateral report required under this section could be made available to the customer or indirect intermediary through either direct electronic access available to the customer or indirect intermediary at any time or a daily report sent to the customer or indirect intermediary.

## **Disclosure of investment of customer collateral**

27. We are of the view that the requirement to provide disclosure under subsection 27(1) and subsection 27(2) may be satisfied by directing a customer or, if applicable, the indirect intermediary to the disclosure on the clearing intermediary's website.

## **PART 5 TREATMENT OF COLLATERAL BY A REGULATED CLEARING AGENCY**

Part 5 contains requirements for the treatment of customer collateral by regulated clearing agencies.

### **Collection of initial margin**

28. The requirement that a regulated clearing agency collect initial margin on a gross basis for each customer means that a regulated clearing agency may not, and may not permit its direct intermediaries to offset initial margin positions of different customers against one another. However, the initial margin collected from a customer may be determined by netting across the various cleared derivative positions of that customer. Further, a regulated clearing agency is not prohibited from collecting variation margin for cleared derivatives on a net basis from its direct intermediaries.

Margin requirements are determined by the regulated clearing agency in accordance with its rules, policies and procedures. For further discussion, please see National Instrument 24-102 *Clearing Agency Requirements* ("NI 24-102") for requirements applicable to clearing agency margin calculation.

### **Segregation of customer collateral – regulated clearing agency**

29. Records maintained by the regulated clearing agency must make it clear that customer accounts are for the benefit of customers only.

We are of the view that parties should have the benefit of flexibility in their collateral arrangements. However, the principle remains that notwithstanding the legal arrangement under which customer collateral is posted with a regulated clearing agency, the regulated clearing agency must treat customer collateral posted with it as belonging to customers. For example, in a title transfer collateral arrangement, where the title to the property posted as collateral is transferred to the person or company collecting the collateral, despite any such transfer of legal title from the customer (or clearing intermediary on behalf of the customer) to a regulated clearing agency, such regulated clearing agency must treat any property transferred as collateral by or on behalf of a customer and relating to that customer's cleared derivatives, as customer collateral and as the property of that customer.

### **Holding of customer collateral – regulated clearing agency**

30. (1) A regulated clearing agency is a permitted depository under the Instrument and therefore may hold collateral itself if it offers depository services and is not required to hold customer collateral at a third-party permitted depository. The customer collateral of multiple customers may be commingled in an omnibus customer account. However, the record-keeping obligations in the Instrument require the regulated clearing agency to identify the positions and collateral held for each individual customer within an omnibus customer account.

We are of the view that a regulated clearing agency that holds customer collateral at a third-party permitted depository in accordance with the Instrument should take reasonable commercial efforts to confirm that the permitted depository:

- qualifies as a permitted depository under the Instrument;

- has appropriate rules, policies and procedures, including robust accounting practices, to help ensure the integrity of the customer collateral and minimize and manage the risks associated with the safekeeping and transfer of the collateral;
- maintains securities in an immobilised or dematerialised form for their transfer by book entry;
- protects customer collateral against custody risk through appropriate rules and procedures consistent with its legal framework;
- employs a robust system that ensures segregation between the permitted depository's own property and the property of its participants and segregation among the property of participants, and where supported by the legal framework, supports operationally the segregation of property belonging to a participant's customers on the participant's books and facilitates the transfer of customer collateral;
- identifies, measures, monitors, and manages its risks from other activities that it may perform; and
- facilitates prompt access to customer collateral, when required.

(2) Subsection 30(2) also requires a regulated clearing agency to hold customer collateral relating to cleared derivatives separately from any other type of customer property, including any other property posted by a customer as collateral relating to another position, investment or financial instrument. For example, the customer collateral of a customer may not be commingled with collateral relating to a futures transaction, or any other property or collateral, of the same customer or of any other customer.

#### **Excess margin – regulated clearing agency**

**31.** We would interpret the requirement that a regulated clearing agency identify and record the excess margin that it holds as only applying to that excess margin. For example, a regulated clearing agency would not be required to keep records relating to excess margin held by a clearing intermediary.

#### **Use of customer collateral – regulated clearing agency**

**32. (2)** Subject to an exception for excess collateral, regulated clearing agencies are only permitted to apply the customer collateral of a customer to the cleared OTC derivatives of that customer. Accordingly, the Instrument prohibits the cross-margining of a customer's OTC derivatives and futures positions. The reasoning for this is that the regulatory framework applicable to futures in certain jurisdictions, including Canada, may make customers more susceptible to shortfalls in the event of a clearing intermediary's insolvency and therefore cross-margining could undermine a customer's ability to port its cleared OTC derivatives positions. However, in some jurisdictions, customer protection requirements applicable to futures are equivalent to those applicable to cleared OTC derivatives; under such regimes cross margining may not represent a material risk to porting a customer's OTC derivatives positions. Therefore, when considering an application for discretionary relief from the prohibition on cross-margining or when making an equivalence determination of a foreign jurisdiction's regulatory requirements for the purpose of substituted compliance, the regulator or securities regulatory authority will take these factors into account.

The use of customer collateral attributable to one customer to satisfy the obligations of another customer is not permitted. Although the customer collateral may be held in one omnibus account, such collateral is not available to satisfy customer obligations generally. Therefore, clearing models which allow recourse to a non-defaulting customer's collateral, including any model that permits fellow customer risk, violates this provision and would not be permitted to be offered to customers. For certainty, fellow customer risk is found in a clearing model that allows the customer collateral of a non-defaulting customer to be used to settle the obligations of a defaulting

customer. The pooling of customer collateral held by a regulated clearing agency pursuant to applicable bankruptcy and insolvency laws would not be considered a use of customer collateral by the regulated clearing agency and is permitted where required by applicable laws.

(3) Subsection 32(3) allows a regulated clearing agency to place a lien on customer collateral where the lien arises in connection with the cleared derivative. This exception recognizes that certain clearing arrangements involve the granting of security interests in customer collateral. A regulated clearing agency is prohibited from imposing or permitting improper liens on customer collateral and should an improper lien be placed on customer collateral, the regulated clearing agency must take all commercially reasonable steps to promptly address the improper lien. However, liens over excess collateral are not restricted where the lien is imposed to secure or extend credit to the customer.

### **Investment of customer collateral – regulated clearing agency**

**33. (3)** Although losses in the value of invested customer collateral are not to be allocated to a customer, we are of the view that parties should be free to contract for the allocation of gains resulting from a regulated clearing agency's investment activities in accordance with the Instrument. Subsection 33(3) provides that any loss resulting from a permitted investment of customer collateral must be borne by the investing regulated clearing agency and not by the customer. Where a regulated clearing agency's rules provide for investment loss mutualisation and allocation to clearing intermediaries, this would not violate the requirement.

This requirement relates only to investments made by a regulated clearing agency using customer collateral, not to collateral provided by a customer. If, for example, a customer provided government bonds as collateral, and those bonds lost market value, the regulated clearing agency would not be required to bear those losses. Similarly, where a customer provided collateral to a regulated clearing agency and it was transformed into government bonds to be used as customer collateral, the regulated clearing agency would not be required to bear any loss in market value of the transformed customer collateral.

### **Use of customer collateral – clearing intermediary default**

**34.** An example of when a regulated clearing agency may apply customer collateral to settle the obligations of a defaulting clearing intermediary is when a customer's default is the root cause of the default of the clearing intermediary, whether directly or through the default of an indirect intermediary. In such case, a regulated clearing agency could use the defaulting customer's collateral, including its customer collateral under the Instrument, to satisfy the clearing intermediary's obligations attributable to the customer's default.

### **Risk management –NI 24-102 applies**

**35.** Once in force, NI 24-102 will apply to all regulated clearing agencies providing clearing services to local customers as opposed to only those clearing agencies that are recognized. Therefore, NI 24-102 will apply to clearing agencies that are exempt from recognition if they clear customer transactions.

## **PART 6 RECORD-KEEPING BY A REGULATED CLEARING AGENCY**

Part 6 outlines the minimum record-keeping requirements that apply to regulated clearing agencies. The effectiveness of the customer protections required under the Instrument is predicated on accurate and thorough record-keeping by regulated clearing agencies.

### **Retention of records – regulated clearing agency**

**36.** The records required to be prepared pursuant to this Part and Part 7 must be retained for at least 7 years and in accordance with record retention practice in Canada and the timing requirements under the limitations acts in each local jurisdiction. Records prepared in relation to a cleared derivative include any customer profiles or other information collected from a customer prior to the date upon which a transaction for the customer is entered into and must be kept for at least 7 years after the date upon which a customer's last cleared derivative expires or terminates.

### **Books and records – regulated clearing agency**

**37. (2)** Paragraph 37(2)(b) requires a description of the customer collateral held at each permitted depository. The description should include an industry standard security identifier such as a CUSIP or ISIN code or, if an identifier is not available, a plain language description of the collateral.

We are of the view that accurate record-keeping requires, at minimum, daily valuations of customer collateral using industry standard best practice methodologies. With respect to records required to be kept under paragraph 37(2)(c):

- subparagraph (i) refers to any revenue generated by the customer collateral, including, for example, dividend pay-outs relating to securities and coupon payments relating to debt instruments;
- subparagraph (ii) refers to any changes in the value of property forming part of the customer collateral, including, for example, an increase or decrease in the value of a security;
- subparagraph (iii) refers to charges that have accrued, or may accrue, against the customer and have been agreed to between the regulated clearing agency and the customer; such charges may include, for example, transaction or currency exchange charges or charges relating to the settlement or termination of a cleared derivative.

### **Separate records – regulated clearing agency**

**38.** A regulated clearing agency has record-keeping obligations relating to all customers for which it clears cleared derivatives.

Paragraph (c) ensures that direct and indirect customers receive equal treatment. Direct intermediaries are required to make this information available to indirect intermediaries to which they provide clearing services pursuant to section 18.

### **Records of investment of customer collateral – regulated clearing agency**

**39.** We are of the view that the requirement in paragraph 39(d) would be fulfilled by providing a unique identifier from an industry-accepted identifying standard, such as an ISIN or CUSIP number or, if an identifier is not available, a plain language description of each instrument or asset.

### **Records of currency conversion – regulated clearing agency**

**40.** We are of the view that currency conversion trade records should include, at minimum, all of the following:

- the identity of the customer as represented by its LEI or the name of the customer where the customer is ineligible for a LEI;

- the date of the currency exchange;
- the amount and original currency of the funds to be exchanged;
- the exchange rate at which the currency exchange is made;
- the amount and new currency resulting from the exchange;
- the name of the institution which made the exchange and/or provided the exchange rate.

## **PART 7 REPORTING AND DISCLOSURE BY A REGULATED CLEARING AGENCY**

Part 7 outlines certain disclosure and reporting to be made by a regulated clearing agency to customers, clearing intermediaries and the local securities regulatory authority. Disclosure required to be provided to customers under this Part is not required on a transaction by transaction basis.

The written disclosure required under sections 41 and 45 is necessary only once upon the opening of each customer account, not prior to each cleared derivative transaction. If there are changes to the information contained in the disclosure a customer received, the customer must be promptly informed in writing of such changes. Where there are multiple clearing intermediaries, a direct intermediary may provide disclosure either to a clearing intermediary closer in the transaction chain to the customer or directly to the customer. Written disclosure and notice of changes to such disclosure can be provided in electronic form by delivering copies of required materials or by providing links to online information to the customer or direct intermediary.

Where a regulated clearing agency is already providing clearing services before the Instrument comes into force, the written disclosure required to be delivered in this Part must be delivered before accepting the first cleared derivative after the Instrument comes into force.

We acknowledge the confidential nature of the information that must be reported to the local securities regulatory authority, and each securities regulatory authority will treat it as such, subject to applicable provisions of the legislation adopted by each province and territory including any applicable freedom of information and protection of privacy legislation. However, information may be shared with self-regulatory organizations or other relevant regulatory authorities.

### **Disclosure to direct intermediaries by regulated clearing agency**

**41. (1)** The information given in the written disclosure should assist customers in: (i) evaluating the level of protection provided, (ii) the manner in which segregation and the transfer of assets is achieved, including the method for determining the value at which customer positions will be transferred, and (iii) any risks or uncertainties associated with such arrangements. Disclosure helps customers assess the related risks and conduct due diligence when entering into transactions that are cleared through a direct intermediary of the regulated clearing agency.

Examples of the information that the disclosure should provide include:

- which bankruptcy and insolvency laws apply and how they may impact the regulated clearing agency's ability, in relation to its clearing intermediaries and customers, to expeditiously terminate such relationships, transfer customer collateral and enforce rights in relation to customer collateral;
- the process for recovering or transferring customer collateral should the clearing intermediary default;

- analysis of applicable laws governing the regulated clearing agency including whether the regulated clearing agency is described or named under the *Payment and Clearing Settlement Act* (Canada);
- how the applicable legal framework protects customer collateral and any risks associated with that framework;
- where a customer is required to take proactive steps to protect its collateral, information on what steps a customer can take to do so such as, filing financing statements under laws regulating the creation and registration of security interests in personal property, such as the *Personal Property Security Act* (Ontario) or such other similar legislation in the local jurisdiction;
- the interaction of domestic and foreign laws applicable to customer collateral held by the regulated clearing agency.

(2) The written disclosure required under subsection 41(1), is necessary only upon the opening of each customer account, or upon any change to the rules, policies or procedures of the regulated clearing agency, rather than prior to each cleared derivative transaction.

#### **Customer information – regulated clearing agency**

42. In order to facilitate a timely transfer of collateral and positions in a default scenario, a regulated clearing agency should receive complete and timely information from a direct intermediary under subsection 24(1) in order to identify each customer of a clearing intermediary, and the customer's positions and customer collateral.

#### **Customer collateral report - regulatory**

43. We are of the view that regular reporting on customer collateral deposits and holdings will assist the provincial securities regulatory authorities in monitoring customer collateral arrangements and developing and implementing rules to protect customer assets that are responsive to market practices. To that end, section 43 sets out reporting requirements for regulated clearing agencies regarding customer collateral. A completed Form 94-102F3 will provide the local securities regulatory authority with a snapshot of the value of collateral held by the regulated clearing agency.

#### **Customer collateral report – direct intermediary**

44. The customer collateral report required under this section could be made available to a direct intermediary through either direct electronic access available to the direct intermediary at any time or a daily report sent to the direct intermediary.

#### **Disclosure of investment of customer collateral**

45. We are of the view that the requirements to provide disclosure under subsection 45(1) and subsection 45(2) may be satisfied by directing a customer to the disclosure on the regulated clearing agency's website.

## **PART 8 TRANSFER OF POSITIONS**

Part 8 provides for the transfer of customer collateral and positions from one clearing intermediary to another, either in a default scenario or upon request of the customer. Part 8 also addresses, in part, the following recommendation included in *CSA Consultation Paper 91-404 – Derivatives: Segregation and Portability in OTC Derivatives Clearing*:

“Each CCP shall have rules facilitating the termination of contractual relationships between a clearing member and its customers and the transfer of positions.”

The efficient and complete transfer of customer collateral and related positions is important in both pre-default and post-default scenarios but is particularly critical when a clearing intermediary defaults or is undergoing insolvency proceedings.

### **Transfer of customer collateral and positions**

**46. (1)** We are of the view that operations, policies and procedure of clearing intermediaries and regulated clearing agencies should be structured to ensure, to the greatest extent possible, that a default by a clearing intermediary does not affect the positions and collateral of the defaulting clearing intermediary’s customers. Generally, default by a direct intermediary would occur when it does not, or is unable to, meet its obligations at a regulated clearing agency.

To ensure that customer collateral and positions are insulated from a direct intermediary’s default, including any winding-up or restructuring proceeding of the defaulting direct intermediary, a regulated clearing agency must be structured, including by having the necessary rules and procedures in place, to effectively and promptly facilitate the transfer of customer collateral and positions to a direct intermediary that (i) is not in default, as that term is defined in the rules and procedures of the relevant regulated clearing agency, and (ii) is not reasonably expected to default on its obligations at a regulated clearing agency as they come due.

We are of the view that customer collateral and positions should be transferred as seamlessly as possible from the perspective of the customer. This means that a customer’s positions should be maintained on identical economic terms as governed the position of such customer immediately before the transfer. We are of the view that, in effecting such a transfer, a regulated clearing agency be permitted to operationally close-out and re-book the positions, provided that the ultimate result is that the customer’s positions are maintained on identical economic terms as governed immediately before the transfer.

The regulated clearing agency’s ability to transfer customer collateral and related positions in a timely manner may depend on such factors as market conditions, sufficiency of information on the individual constituents, and the complexity or size of the customers’ portfolio. The regulated clearing agency should therefore structure its arrangements for the transfer of customer collateral and positions in a way that makes it highly likely that they will be effectively transferred to one or more other direct intermediaries, taking into account all relevant circumstances. In order to achieve a high likelihood of transferability, the regulated clearing agency will need to have the ability to (i) identify positions that belong to customers, (ii) identify and assert the regulated clearing agency’s rights to related customer collateral held by or through the regulated clearing agency, (iii) transfer positions and related customer collateral to one or more other direct intermediaries, (iv) identify potential direct intermediaries to accept the positions, (v) disclose relevant information to such direct intermediaries so that they can evaluate the counterparty credit and market risk associated with the customers and positions, respectively, and (vi) facilitate the regulated clearing agency’s ability to carry out its default management procedures in an orderly manner. The regulated clearing agency’s policies and procedures should provide for the proper handling of customer collateral and related positions of customers of a defaulting direct intermediary.

Although we stress the importance of the transfer of customer collateral and positions in a default scenario, we acknowledge that there may be circumstances where the portability of all or a portion of a customer’s position is not possible. Where a regulated clearing agency is not able to transfer positions within a pre-defined transfer period specified in its operating rules, it may take all steps permitted by its rules to actively manage its risks in relation to those positions, including liquidating the customer collateral and positions of the defaulting direct intermediary’s customers.

We are of the view that a direct intermediary should also have policies and procedures in place to facilitate the prompt transfer of customer collateral that it holds to one or more direct intermediaries in the event of its own default.

(2) A regulated clearing agency must be structured, including by having the necessary rules and procedures in place, to facilitate the transfer of the customer collateral and positions of a customer from one direct intermediary to another at the request of the customer. This is also known as a “business-as-usual transfer”.

A customer should be able to transfer its customer collateral and positions to another direct intermediary in the normal course of business. Subsection 46(2) requires that a regulated clearing agency be structured, including by having the necessary rules and procedures in place, to facilitate the transfer of customer collateral and related positions upon the customer’s request to any one or more non-defaulting direct intermediaries, subject to any notice or other contractual requirements.

(3) Where a transfer of customer collateral and positions is facilitated under subsection 46(1) or 46(2), a regulated clearing agency may promptly transfer the customer’s positions and related customer collateral, as a single portfolio or in portions, as requested by the customer, to one or more direct intermediaries.

Subsection 46(3) sets out certain pre-conditions for the transfer of customer collateral and positions, in either a default or business-as-usual transfer. The regulated clearing agency must obtain the consent of the customer with respect to the transfer of the customer collateral and positions of the customer to the particular transferee direct intermediary. We are of the view that this consent may be best obtained at the outset of a clearing relationship, and by allowing a customer to identify direct intermediaries to which it consents *a priori* to such a transfer. If there are circumstances where this consent would not be obtained, or where the prior consent would not be followed, those circumstances should be set out in the rules, policies or procedures of the regulated clearing agency.

The regulated clearing agency must also obtain the consent of the receiving direct intermediary as to which positions and customer collateral are to be transferred. We are of the view that the consent of the direct intermediary is also best obtained at the outset of the customer’s relationship with the regulated clearing agency. If there are circumstances where the consent of the direct intermediary would not be obtained *a priori* to a transfer, those circumstances should be set out in the rules, policies or procedures of the regulated clearing agency.

### **Transfer from a clearing intermediary**

47. We are of the view that customers of a clearing intermediary should benefit from protections and rights under the Instrument, with respect to the transfer of positions and collateral. To that end, in the event of the clearing intermediary’s default, the clearing intermediary must be structured to promptly facilitate such a transfer, as a single portfolio or in portions as requested by the customer, to one or more non-defaulting clearing intermediaries.

## **PART 9 SUBSTITUTED COMPLIANCE**

48. (1) Subsection 48(1) contemplates substituted compliance by foreign clearing intermediaries that are regulated under the laws of a foreign jurisdiction that achieve substantially the same objectives as the Instrument. Substituted compliance will only apply to the provisions of the Instrument specified in Appendix A where the clearing intermediary is in compliance with the corresponding laws of the foreign jurisdiction set out next to such provision of the Instrument in Appendix A. The provisions specified for substituted compliance will be determined on a jurisdiction by jurisdiction basis, and will depend on a review of the laws and regulatory framework of the foreign jurisdiction.

(2) Subsection 48(2) contemplates substituted compliance by foreign regulated clearing agencies that are recognized or exempt from recognition by a Canadian securities regulatory authority and are in compliance with the laws of a foreign jurisdiction that achieve substantially the same objectives as the Instrument. Substituted compliance will only apply to the provisions of the Instrument specified in Appendix A where the regulated clearing agency is in compliance with the corresponding laws of the foreign jurisdiction set out next to such provision of the Instrument in Appendix A.