

# **2003 BCSECCOM 391**

## **Headnote**

Mutual Reliance Review System for Exemptive Relief Application – relief from registration and prospectus requirements for trades in over-the-counter derivatives between qualified parties

## **Applicable British Columbia Provisions**

*Securities Act*, R.S.B.C.1996, c. 418, ss. 48 and 76

**IN THE MATTER OF THE CANADIAN SECURITIES LEGISLATION OF  
ALBERTA, BRITISH COLUMBIA, MANITOBA, NEW BRUNSWICK,  
NEWFOUNDLAND AND LABRADOR, NOVA SCOTIA, ONTARIO,  
PRINCE EDWARD ISLAND, QUEBEC, SASKATCHEWAN, THE  
YUKON, THE NORTHWEST TERRITORIES AND THE NUNAVUT  
TERRITORY**

**AND**

**IN THE MATTER OF THE MUTUAL RELIANCE REVIEW SYSTEM  
FOR EXEMPTIVE RELIEF APPLICATIONS**

**AND**

**IN THE MATTER OF TD COMMODITY & ENERGY TRADING INC.**

## **MRRS DECISION DOCUMENT**

WHEREAS the local securities regulatory authority or regulator (Decision Maker) in each of the provinces and territories of Canada (collectively, the Jurisdictions) has received an application from TD Commodity & Energy Trading Inc. (Applicant) for a decision under the securities legislation of the Jurisdictions (the Legislation) that (i) the requirements in the Legislation to be registered to trade in a security (Registration Requirement) and to file and obtain a receipt for a preliminary prospectus and a prospectus in respect of such security (Prospectus Requirement) shall not apply to trades in over-the-counter (OTC) derivatives entered into between the Applicant and certain counterparties, and (ii) any fees required to be paid under the Legislation in respect of such OTC derivatives transactions shall not be required to be paid in the Jurisdictions;

AND WHEREAS pursuant to the Mutual Reliance Review System for Exemptive Relief Applications (the System) the Ontario Securities Commission is the principal regulator for this application;

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AND WHEREAS, unless otherwise defined, the terms herein have the meaning set out in National Instrument 14-101 Definitions or in Québec Commission Notice 14-101;

AND WHEREAS the Applicant has represented to the Decision Makers that:

1. The Applicant is a corporation organized under the laws of Canada. The Applicant is a direct, wholly-owned subsidiary of TD Securities Inc. (TD Securities). TD Securities is a direct, wholly-owned subsidiary of The Toronto-Dominion Bank (TD Bank), a bank listed on Schedule I of the *Bank Act* (Canada). TD Securities is registered under the Legislation as a dealer in the categories of “broker” and “investment dealer” and is a member of the Investment Dealers Association of Canada.
2. The head office of the Applicant is located in Calgary, Alberta. The Applicant is not registered as a dealer or adviser under the securities legislation in any province or territory of Canada. The Applicant is also not a reporting issuer in any province or territory of Canada.
3. The Applicant proposes to design, create and market a full range of commodity-related derivative products that address the broad operational, risk management and investment needs of its clients. Such derivative products may also include interest rate, foreign exchange, equity and credit-related components and will be settled either physically or in cash.
4. The Applicant will originate and market all of the Applicant’s derivative products business and both the Applicant and its affiliates will act as counterparties to the Applicant’s clients in respect of both cash and physically settled derivative products.
5. The Applicant is proposing to engage in the marketing and trading of OTC derivatives with certain counterparties in the Jurisdictions. The OTC derivatives in which the Applicant proposes to transact are designed on a case-by-case basis to fit the needs of the particular client. These OTC derivatives will consist of one or more of an option, a forward contract, a swap or a contract for differences of a type commonly considered to be a derivative, in which:
  - (a) the agreement relating to, and the material economic terms of the option, forward contract, swap or contract for differences have been customized to the purposes of the parties to the agreement and the agreement is not part of a fungible class of agreements that are standardized as to their material economic terms;

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- (b) the creditworthiness of a party having an obligation under the agreement would be a material consideration in entering into or determining the terms of the agreement; and
  - (c) the agreement is not entered into or traded on or through an organized market, stock exchange or futures exchange and is not cleared by a clearing corporation.
- 6. The underlying interest of the OTC derivatives transacted between the Applicant and the counterparties will consist entirely of a commodity, an interest rate, a foreign exchange rate, a security, an index, a benchmark or other variable, another OTC derivative, or some relationship between, or combination of, one or more of any of them.
- 7. The counterparties to such transactions will consist exclusively of parties that meet the following criteria:
  - (a) they are Qualified Parties, as defined in Appendix 1 to this MRRS Decision Document;
  - (b) they have a high level of business and financial sophistication;
  - (c) they have access to their own in-house or external advisors who can assist in the determination of the suitability of the transaction and the creditworthiness of the Applicant; and
  - (d) in the ordinary course of their businesses (or investing activity), they enter into OTC derivative trades in order to hedge or otherwise manage specific risks.

AND WHEREAS pursuant to the System this MRRS Decision Document evidences the decision of the Decision Makers (the Decision);

AND WHEREAS each of the Decision Makers is satisfied that the test contained in the Legislation that provides the Decision Maker with the jurisdiction to make the Decision has been met;

THE DECISION of the Decision Makers under the Legislation is that the Applicant and the Applicant's counterparties who are Qualified Parties shall each be exempt from the Registration Requirement and the Prospectus Requirement in respect of trades in OTC derivatives subject to the following conditions:

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- (i) each trade involves an OTC derivative of which the underlying interest consists entirely of a commodity, an interest rate, a foreign exchange rate, a security, an index, a benchmark or other variable, or another OTC derivative, or some relationship between, or combination of, one or more of any of them; and
- (ii) each trade is marketed by the Applicant and is between either the Applicant and a Qualified Party or two Qualified Parties, each acting as principal.

AND THE FURTHER DECISION of the Decision Maker of Ontario under the Legislation is that trades entered into in reliance on this Decision are hereby exempted from the fees which would otherwise be payable in connection with such OTC derivative transactions pursuant to the Legislation.

DATED this 9<sup>th</sup> day of June, 2003

H. P. Hands

H. L. Morphy

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## Appendix A

### OVER-THE-COUNTER DERIVATIVES QUALIFIED PARTIES

#### Interpretation

- (1) The terms “subsidiary” and “holding body corporate” used in paragraphs (w), (x) and (y) of subsection (3) of this Appendix have the same meaning as they have in the *Business Corporations Act* (Ontario).
- (2) All requirements contained in this Appendix that are based on the amounts shown on the balance sheet of an entity apply to the consolidated balance sheet of the entity.

#### Qualified Parties Acting as Principal

- (3) The following are Qualified Parties for all OTC derivatives transactions, if acting as principal:

##### *Banks*

- (a) A bank listed in Schedule I or II to the *Bank Act* (Canada).
- (b) The Business Development Bank of Canada incorporated under the *Business Development Bank of Canada Act* (Canada).
- (c) A bank subject to the regulatory regime of a country that is a member of the Basle Accord, or that has adopted the banking and supervisory rules set out in the Basle Accord, if the bank has a minimum paid up capital and surplus, as shown on its last audited balance sheet, in excess of \$25 million or its equivalent in another currency.

##### *Credit Unions and Caisses Populaires*

- (d) A credit union central, federation of caisses populaires, credit union or regional caisse populaire, located, in each case, in Canada.

##### *Loan and Trust Companies*

- (e) A loan corporation or trust corporation registered under the *Loan and Trust Corporations Act* (Ontario) or under the *Trust and Loan Companies*

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Act (Canada), or under comparable legislation in any other province or territory of Canada.

- (f) A loan company or trust company subject to the regulatory regime of a country that is a member of the Basle Accord, or that has adopted the banking and supervisory rules set out in the Basle Accord, if the loan company or trust company has a minimum paid up capital and surplus, as shown on its last audited balance sheet, in excess of \$25 million or its equivalent in another currency.

### *Insurance Companies*

- (g) An insurance company licensed to do business in Canada or a province or territory of Canada;
- (h) An insurance company subject to the regulatory regime of a country that is a member of the Basle Accord, or that has adopted the banking and supervisory rules set out in the Basle Accord, if the insurance company has a minimum paid up capital and surplus, as shown on its last audited balance sheet, in excess of \$25 million or its equivalent in another currency.

### *Sophisticated Entities*

- (i) A person or company that, together with its affiliates:
  - (i) has entered into one or more transactions involving OTC derivatives with counterparties that are not its affiliates, if
    - (A) the transactions had a total gross dollar value of or equivalent to at least \$1 billion in notional principal amount; and
    - (B) any of the contracts relating to one of these transactions was outstanding on any day during the previous 15-month period, or
  - (ii) had total gross marked-to-market positions of or equivalent to at least \$100 million aggregated across counterparties, with counterparties that are not its affiliates in one or more transactions involving OTC derivatives on any day during the previous 15-month period.

### *Individuals*

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- (j) An individual who, either alone or jointly with the individual's spouse, has a net worth of at least \$5 million, or its equivalent in another currency, excluding the value of his or her principal residence.

### *Governments/Agencies*

- (k) Her Majesty in right of Canada or any province or territory of Canada and each crown corporation, instrumentality and agency of a Canadian federal, provincial or territorial government.
- (l) A national government of a country that is a member of the Basle Accord, or that has adopted the banking and supervisory rules set out in the Basle Accord, and each instrumentality and agency of that government or corporation wholly-owned by that government.

### *Municipalities*

- (m) Any Canadian municipality with a population in excess of 50,000 and any Canadian provincial or territorial capital city.

### *Corporations and other Entities*

- (n) A company, partnership, unincorporated association or organization or trust, other than an entity referred to in paragraph (a), (b), (c), (d), (e), (f), (g) or (h), with total revenue or assets in excess of \$25 million or its equivalent in another currency, as shown on its last financial statement, to be audited only if otherwise required.

### *Pension Plan or Fund*

- (o) A pension fund that is regulated by either the Office of the Superintendent of Financial Institutions (Canada) or a provincial pension commission, if the pension fund has total net assets, as shown on its last audited balance sheet, in excess of \$25 million, provided that, in determining net assets, the liability of a fund for future pension payments shall not be included.

### *Mutual Funds and Investment Funds*

- (p) A mutual fund or non-redeemable investment fund if each investor in the fund is a Qualified Party.

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- (q) A mutual fund that distributes its securities in any of the Jurisdictions, if the portfolio manager of the fund is registered as an adviser, other than a securities adviser, under any of the Legislation.
- (r) A non-redeemable investment fund that distributes its securities in any of the Jurisdictions, if the portfolio manager of the fund is registered as an adviser, other than a securities adviser, under any of the Legislation.
- (s) A mutual fund or non-redeemable investment fund established and located outside Canada that distributes its securities primarily abroad and only distributes its securities in Canada in reliance upon exemptions from the prospectus requirements of the Legislation.

### *Brokers/Investment Dealers*

- (t) A person or company registered under the Legislation or securities legislation elsewhere in Canada as a broker or an investment dealer or both.
- (u) A person or company registered under the Legislation as an international dealer if the person or company has total assets, as shown on its last audited balance sheet, in excess of \$25 million or its equivalent in another currency.

### *Futures Commission Merchants*

- (v) A person or company registered under the CFA as a dealer in the category of futures commission merchant, or in an equivalent capacity elsewhere in Canada.

### *Affiliates*

- (w) A wholly-owned subsidiary of any of the organizations described in paragraph (a), (b), (c), (d), (e), (f), (g), (h), (j), (n), (o), (t), (u) or (v).
- (x) A holding body corporate of which any of the organizations described in paragraph (w) is a wholly-owned subsidiary.
- (y) A wholly-owned subsidiary of a holding body corporate described in paragraph (x).



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- (z) A firm, partnership, joint venture or other form of unincorporated association in which one or more of the organizations described in paragraph (w), (x) or (y) have a direct or indirect controlling interest.

### *Guaranteed Party*

- (aa) A party whose obligations in respect of the OTC derivatives transaction for which the determination is made is fully guaranteed by another Qualified Party.

### **Qualified Party Not Acting as Principal**

- (4) The accounts of a person, company, pension fund or pooled fund trust that are fully managed by a portfolio manager or financial intermediary referred to in paragraphs (a), (d), (e), (g), (t), (u), (v) or (x) of paragraph (3) or a broker or investment dealer acting as a trustee or agent for the person, company, pension fund or pooled fund trust under section 148 of the Ontario Regulation are Qualified Parties, in respect of all OTC derivative transactions.

### **Subsequent Failure to Qualify**

- (5) A party is a Qualified Party for the purpose of any OTC derivatives transaction if it, he or she is a Qualified Party at the time it, he or she enters into the transaction.

### **Qualified Party for Specified Commodity Derivative Transaction**

- (6) A commercial user is a Qualified Party with respect to any specified commodity derivative transaction. For these purposes:

“commercial user” means a person or company that enters into a specified commodity derivative transaction, if

- (a) the person or company deals in its business with a specified commodity, and
- (b) the transaction involves a specified commodity derivative of which the underlying interest, or a material component of the underlying interest, is
  - (i) a specified commodity referred to in paragraph (a),
  - (ii) a related specified commodity to a specified commodity referred to in paragraph (a), or

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(iii) a specified commodity derivative, the underlying interest of which is

- A. a specified commodity, or
- B. a related specified commodity to a specified commodity referred to in paragraph (a);

“related specified commodity” means a specified commodity that is part or all of an underlying interest of a specified commodity derivative that is used by a commercial user to hedge its exposure to a risk resulting from its use of another specified commodity in its business;

“specified commodity” means

- (a) whether in the original or a processed state, an agricultural product, forest product, product of the sea, mineral, metal, hydrocarbon fuel product or precious stone or other gem,
- (b) a pollutant emission level,
- (c) electricity,
- (d) a liability from an insurance contract, and
- (e) a matter designated by the Commissions as a specified commodity, if that designation has not been revoked; and

“specified commodity derivative” means an OTC derivative of which an underlying interest is:

- (a) a specified commodity, or
- (b) another OTC derivative of which the underlying interest is a specified commodity.