SUTHERLAND ASBILL & BRENNAN LLP
700 Sixth Street, NW, Suite 700
Washington, DC 20001-3980
202.383.0100 Fax 202.637.3593
www.sutherland.com

March 24, 2015

VIA ELECTRONIC MAIL

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Financial and Consumer Services Commission (New Brunswick)
Nova Scotia Securities Commission

c/o:
Mr. Michael Brady
Senior Legal Counsel, Capital Markets
British Columbia Securities Commission
P.O. Box 10142 Pacific Centre
701 West Georgia Street
Vancouver, British Columbia
V7Y 1L2
mbrady@bcsc.bc.ca

Re: Proposed Multilateral Instrument 91-101 Derivatives: Product Determination and Proposed Multilateral Instrument 96-101 Trade Repositories and Derivatives Data Reporting

Dear Sir or Madam:

On behalf of The Canadian Commercial Energy Working Group (the "**Working Group**"), Sutherland Asbill & Brennan LLP hereby submits these comments in response to the request for public comment on (i) Proposed Multilateral Instrument 91-101 Derivatives: Product Determination (the "**Proposed Scope Rule**"), and (ii) Proposed Multilateral Instrument 96-101 Trade Repositories and Derivatives Data Reporting (the "**Proposed TR Rule**") (collectively the "**Proposed Reporting Rules**").[1] The Working Group welcomes the opportunity to provide comments on the Proposed Reporting Rules and looks forward to working with Canadian regulators to help finalize reporting rules responsive to the specific needs of the Canadian derivatives market.

[1] *See* CSA Multilateral Notice and Request for Comment (Jan. 21, 2015), *available at* http://www.albertasecurities.com/Regulatory%20Instruments/5042659-v1-CSA_Notice_and_RFC_on_Proposed_MI_91-101_and_96-101_91.101.pdf.

The Working Group is a diverse group of commercial firms that are active in the Canadian energy industry whose primary business activity is the physical delivery of one or more energy commodities to others, including industrial, commercial, and residential consumers. Members of the Working Group are producers, processors, merchandisers, and owners of energy commodities. The Working Group considers and responds to requests for comment regarding developments with respect to the trading of energy commodities, including derivatives, in Canada.

I. INTRODUCTION.

The Working Group appreciates the regulatory authorities in Alberta, British Columbia, New Brunswick, Nova Scotia, and Saskatchewan (the "**Participating Jurisdictions**") publishing Proposed Reporting Rules that, in all but a few circumstances, are not materially different from the final reporting rules issued in Manitoba, Ontario, and Quebec.[2] In addition, the Working Group appreciates that the Proposed Reporting Rules' proposed regulatory paradigm mirrors the derivatives reporting paradigm in the United States, and thus may prevent unnecessary burdens on market participants. With a few changes, the Proposed Reporting Rules would establish a derivatives reporting paradigm that provides regulators with the necessary transparency into derivatives markets without imposing undue burdens on derivatives market participants.

II. COMMENTS OF THE WORKING GROUP.

A. The Participating Jurisdictions Should Provide Additional Guidance on Who Qualifies as a "Derivatives Dealer."

The Proposed TR Rule defines "derivatives dealer" as "a person or company engaging in or holding himself, herself, or itself out as engaging in the business of trading in derivatives as principal or agent."[3] The Proposed TR Rule's Companion Policy, however, does not provide additional guidance on the factors or the level of activity that would cause an entity to be deemed by the Participating Jurisdictions as "engaging in or holding himself, herself, or itself out" as a derivatives dealer. Without additional guidance, it is unclear who would qualify as a derivatives dealer for the purposes of the Proposed TR Rule.

Moreover, it is also unclear if the determination of whether an entity is a derivatives dealer for the purpose of the Proposed TR Rule is conducted on a transaction-level basis or if the analysis is based on an entity's derivatives activity in the aggregate. Said another way, if an entity is acting like a derivatives dealer with respect to a particular transaction, is it required to report that transaction as a derivatives dealer? Or, is the determination of whether an entity must report as a derivatives dealer for a particular transaction dependent on that entity's aggregate derivatives activity?

---

[2] In each of Manitoba, Ontario, and Quebec, the corresponding rule to the Proposed Scope Rule is Rule 91-506 and the corresponding rule to the Proposed TR Rule is Rule 91-507.

[3] Proposed TR Rule at Section 1(1).

The Proposed TR Rule's Companion Policy adds to the uncertainty when it states "the definition of 'derivatives dealer' in the Instrument does not require that a person or company be registered with the local securities regulatory authority in order to meet the definition. Accordingly, where the reporting counterparty to a transaction is a derivatives dealer, as defined in the Instrument, the reporting obligations with respect to the transaction apply irrespective of whether the derivatives dealer is a registrant in the local jurisdiction."[4] If this language and the current definition of "derivatives dealer" remain in place once derivatives dealer registration rules are finalized, there could be a conflict between the reporting rules and the registration rules.

As such, the Working Group views the statement above and the proposed definition of "derivatives dealer" as addressing two issues. *First*, stating that, under the Proposed TR Rule, registration as a derivatives dealer is not required for a person to be considered a derivatives dealer is necessary since there are currently no rules in place requiring relevant entities to register as a derivatives dealer.

Second, stating that, under the Proposed TR Rule, registration as a derivatives dealer in a particular province is not required for a person to be considered a derivatives dealer is necessary to effectuate the desired approach to the reporting hierarchy, without requiring derivatives dealers to register as such in each province where they have counterparties.

However, the Working Group is concerned that once the dealer registration rules are in place, the language cited above may be read to require an entity that is not registered as a derivatives dealer to report derivatives as if it were one, giving credence to the previously mentioned transaction-level approach and imposing regulatory burdens on entities not otherwise regulated as dealers.

The Working Group respectfully suggests that the proper analytic approach to determine who qualifies as a dealer is at the aggregate-level. A transaction-by-transaction determination would be difficult and burdensome to administer. As an initial matter, the Working Group recommends that, once final derivatives dealer registration rules are in place, the Participating Jurisdictions amend the definition of "derivatives dealer" in the Proposed TR Rule to capture only an entity that is registered or required to register as a derivatives dealer in a Canadian jurisdiction under the criteria to be set forth in the yet-to-be released final rules requiring derivatives dealer registration. In addition, the Participating Jurisdictions should indicate they plan on amending the Proposed TR Rule derivatives dealer definition in such a manner in the final version of the Proposed TR Rule.

In addition, to provide necessary clarity to market participants on how to conduct an aggregate-level derivatives dealer determination, the Participating Jurisdictions should provide a *de minimis* exception. Specifically, the Participating Jurisdictions should allow entities that engage in derivatives dealing below a certain level to avoid registration and reporting as a derivatives dealer. The Working Group understands that the Participating Jurisdictions will not be able to provide a *de minimis* exception until the registration rules are addressed, but requests that the Participating Jurisdictions do the following if they publish final reporting rules prior to

[4] Proposed TR Companion Policy at Section 25(1).

proposed registration rules: (i) indicate that they are planning on providing a *de minimis* exception in any final reporting rules; and (ii) provide an indication as to the order of magnitude of the level of the exception in any final reporting rules. Such an indication would allow market participants to better anticipate their potential derivatives reporting obligations.

B. The Proposed TR Rule's Public Dissemination Requirement Needs Amendments to Provide Market Participants Necessary Protection.

The Proposed TR Rule requires recognized trade repositories to make available to the public certain transaction-specific information for each derivatives transaction required to be reported under the Proposed Reporting Rules, such as underlying commodity, volume, and price.[5]

Pursuant to the Proposed TR Rule, depending on the counterparty, data must be publicly disseminated by either (i) the end of the day following the day on which a recognized trade repository receives the data, or (ii) by the end of the second day following the day on which a recognized trade repository receives the data.[6] The stated purpose of the public reporting delays is to "ensure that counterparties have adequate time to enter into any offsetting transaction that may be necessary to hedge their positions."[7]

The Proposed TR Rule, however, only provides the time frame by which the data must be publicly disseminated and does not provide a minimum time that the data must be held prior to public dissemination. As currently drafted, the Proposed TR Rule would allow a recognized trade repository to publicly disseminate the data as soon as it is received, which would defeat the purpose of the delay and, as discussed further below, would pose risks to market integrity similar to those seen in the United States.

As the Participating Jurisdictions are likely aware, a similar framework for real-time public dissemination was implemented in the United States under the Commodity Futures Trading Commission's ("**CFTC**") regulations.[8] That framework has raised a number of issues for market participants. U.S. market participants' primary concerns are related to the potential disclosure of the identity of counterparties and, in less liquid markets, exposure of counterparties to "front-running" of hedging activity by market participants and the possibility that the public transaction-level data will make it more difficult for counterparties to execute a desired trading strategy.

Specifically, the time delays provided in the CFTC's Real-Time Reporting Rules "are not sufficient for illiquid markets."[9] For example, the Treasurer of Southwest Airlines Co.

---

5 Proposed TR Rule at Section 39.

6 *See* Proposed TR Rule at Section 39(3).

7 Proposed TR Companion Policy at Section 39(3).

8 The CFTC's regulations on real-time reporting are found in Part 43 of the CFTC Regulations, 17 C.F.R. Part 43 ("**CFTC's Real-Time Reporting Rules**").

9 *See* Testimony of Chris Monroe, Treasurer of Southwest Airlines Co., Before the U.S. House of

("**Southwest**") testified in a Congressional hearing that the inadequate reporting delays could cost Southwest $60 million in annual costs and stated that non-counterparty dealers "plainly were aware of trades [Southwest] had entered into…."[10]

The CFTC responded to these concerns by issuing a no-action letter, which provided a 15-day time delay for the public dissemination of certain swaps the CFTC deemed susceptible to the risk of "front-running."[11]

Finally, the Proposed TR Rule requires recognized trade repositories to ensure that their publicly disclosed data is anonymized.[12] Recognized trade repositories, however, are not required to determine whether anonymized published data could reveal the identity of a counterparty based on the terms of the transaction.[13] For example, disclosure of the value of trades with large notional values in certain commodities can provide enough information to the market so that hedging such transactions can become uneconomical.

As such, the Working Group respectfully requests that the Participating Jurisdictions provide a time before which transaction-level data may not be publicly disseminated. That time should be established based on the liquidity of the relevant commodity. The 15-day time delay provided to Southwest by the CFTC was for transactions in the WTI and Brent derivatives, both of which are considered relatively liquid markets, even at the two-year tenor covered by the CFTC's no-action relief. Accordingly, less liquid markets such as WCS may need longer delays, while more liquid markets like CAD Libor-based interest rate swaps may require shorter delays.

In addition, the Working Group respectfully requests that the Participating Jurisdictions provide trade repositories with additional parameters and guidance on how they must treat transaction-level data released to the public to ensure that "anonymized" data published by a trade repository does not reveal the identity of a counterparty to a large notional trade based on the terms of a transaction.

C. Differences Between the Proposed TR Rule's Reporting Hierarchy and Ontario's Reporting Hierarchy Must Be Resolved.

The Proposed TR Rule establishes a hierarchy to determine which counterparty to a derivatives transaction must report the data with respect to that transaction. That hierarchy is

---

Representatives Committee on Agriculture, Subcommittee on General Farm Commodities and Risk Management at 2 (July 24, 2013), *available at* http://agriculture.house.gov/sites/republicans.agriculture.house.gov/files/pdf/hearings/Monroe130724.pdf.

[10] *Id.*

[11] CFTC No-Action Letter 14-134, Division of Market Oversight, *Time Limited No-Action Relief: Further Time Delay for Public Dissemination of Long-dated Brent and WTI Crude Oil Swap and Swaption Contracts Executed by or with Southwest Airlines* (Nov 6, 2014), *available at* http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-134.pdf.

[12] Proposed TR Rule at Section 39(4).

[13] Proposed TR Companion Policy at Section 39(4).

workable for commercial energy firms and is consistent with the reporting rules in Manitoba and Quebec. However, portions of the proposed hierarchy are inconsistent with the Ontario Securities Commission's ("**OSC**") reporting rules.[14] Specifically, there are material differences with the OSC TR Rule and the Proposed TR Rule regarding the manner in which counterparties that are at the same level of the reporting hierarchy may assign reporting responsibility and allow the non-reporting counterparty to avoid regulatory liability.

Under the OSC TR Rule, reporting liability can only be avoided if the counterparties sign on to an International Swaps and Derivatives Association ("**ISDA**") multilateral agreement and adhere to the ISDA methodology.[15] Requiring the use of the ISDA methodology and execution of the ISDA multilateral agreement is an unworkable solution for many derivatives market participants.

In particular, to determine the reporting counterparty under the ISDA methodology, the counterparties must first look to their regulatory status under the CFTC's regulations to determine the reporting counterparty. If the counterparties have the same regulatory status in both Canada and the United States, then the counterparties would look to the ISDA methodology's "tie-breaker logic." For commodities-based derivatives, the "tie-breaker logic" would generally require the "seller" in a transaction to serve as the reporting counterparty.

ISDA's tie-breaker logic is likely not helpful for end-user counterparties that have the same regulatory status in Canada and the United States. Specifically, the tie-breaker language presupposes that both counterparties to a derivatives trading relationship are able to report derivatives to a trade repository, as the role of "seller" can switch back and forth between the counterparties from transaction to transaction. In trading relationships between two end-users, it is possible that one of the counterparties will not have the ability to report derivatives. As such, one counterparty may have to serve as the permanent reporting counterparty, eliminating the ISDA methodology as a viable choice and requiring the non-reporting counterparty to retain its reporting requirement liability under the OSC's TR Rule.

Under the Proposed TR Rule, however, counterparties with the same reporting hierarchy status have more flexibility because they may simply agree to assign the reporting liability to one of the counterparties by written contract. The Working Group respectfully requests that the Participating Jurisdictions provide further clarity on how a local counterparty's transactions would be impacted if the other party is a local counterparty in Ontario and subject to the ISDA methodology.

Given the differences between the OSC's TR Rule and the Proposed TR Rule, end-users without the ability to report derivatives transactions that involve local counterparties in Ontario are at a disadvantage when compared to how end-users in the Participating Jurisdictions would be treated under the Proposed TR Rule. As such, the Working Group requests that the regulators

---

[14] The OSC's reporting rules are Rule 91-506 ("**OSC Scope Rule**") and Rule 91-507 ("**OSC TR Rule**") (collectively, the "**OSC Reporting Rules**").

[15] *Compare* Section 25 of the OSC TR Rule *with* Section 25 of the Proposed TR Rule.

in the Participating Jurisdictions work with the OSC to amend the OSC's TR Rule to reflect the more flexible reporting hierarchy paradigm set forth in the Proposed TR Rule.

D. The Proposed TR Rule's Exclusion for End-Users from Reporting Trades of Commodity Derivatives Needs Clarification with Respect to the Threshold.

i. Overview.

The Proposed TR Rule provides end-users with two options to qualify for an exclusion from the reporting of commodity derivatives, if certain conditions are met. The Working Group welcomes the Participating Jurisdictions' proposed end-user exclusion from the reporting requirements and, with certain changes, Option 1 in Section 40 of the Proposed TR Rule could provide meaningful relief to commodity derivatives end-users.

The exclusion from reporting requirements under Option 1 applies between two end-users (*e.g.*, entities that are not derivatives dealers or Canadian financial institutions) if each counterparty to the transaction has, at the time of the transaction, outstanding commodity derivatives transactions with less than $250 million aggregate gross notional value, including the notional value related to the new transaction.[16]

Option 2 would apply between two end-users when the local counterparty has, at the time of the transaction, less than $500,000 aggregate gross notional value under all outstanding derivatives transactions, including the additional notional value related to that transaction. As previously noted by derivatives end-users, the threshold in Option 2 is too low to provide meaningful relief.[17] [18]

ii. The Notional Value Threshold.

The use of a notional value-based threshold in Option 1 raises two issues. *First*, the Proposed TR Rule does not provide guidance on how to calculate the notional value of commodity derivatives. The calculation of notional value for commodity derivatives is not as straightforward as it is for other derivatives. The notional value of commodity derivatives is a function of the notional volume of the underlying commodity and not a notional dollar amount, as used for other products.

---

[16] *See* Proposed TR Rule at Section 40; *see also* Proposed TR Companion Policy at Section 40.

[17] Shell Energy North America (Canada) Inc., Shell Trading Company comment letter, *Canadian Securities Administrators ("CSA") Consultation Paper 91-301 Model Provincial Rules – Derivatives: Product Determination, and Trade Repositories and Derivatives Data Reporting* (February 4, 2013) *available at*: http://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20130204_91-301_kerrp.pdf.

[18] Suncor Energy Inc. comment letter, *Comment Letter to CSA Staff Consultation Paper 91-301 – Model Provincial Rules – Derivatives; Product Determination and Trade Repositories and Derivatives Data Reporting* (February 4, 2013) *available at*: https://www.osc.gov.on.ca/documents/en/Securities-Category9-Comments/com_20130204_91-301_serrac.pdf.

For example, the notional value of a $100 million interest rate swap is $100 million. However, the notional value of a swap based on 100,000 barrels of crude oil is a function of the price of that crude oil. With that in mind, the Working Group respectfully recommends the Participating Jurisdictions adopt the following approach for calculating the notional value of a derivative:

- For a fixed price for floating price commodity swap, the notional value would be the difference between the two prices at calculation * total volume of the contract.

- For a floating price commodity swap, the notional value would be the difference between the two prices at calculation * total volume of the contract.

- For an option, the notional value would be the premium * the total volume of the option.

Second, the use of a counterparty's gross notional value of outstanding commodity derivatives, at the time of execution of a transaction, as the relevant threshold for the reporting exclusion will be difficult to implement given the volatility in commodity prices. For example, a refiner that has the capacity to refine 2 million barrels of Canadian crude oil a month, or 24 million barrels a year, in its U.S. refineries could enter into WCS/WTI basis swaps[19] to hedge its crude oil needs for the next year throughout the current year. If the current price differential between WCS and WTI was $10, that entity would qualify for the proposed exclusion from reporting in the Proposed TR Rule since its notional value would be $240 million. However, if the differential between WCS and WTI reached $15 or even $11, that entity's notional value may no longer qualify for the proposed exclusion based solely on factors outside of its control. As such, if the refiner would like to access the full universe of available counterparties, it must build out its derivatives reporting infrastructure in anticipation of potentially losing the exclusion overnight.

To provide more effective relief for end-users, the Working Group recommends that the Participating Jurisdictions amend Option 1 to provide a reporting exclusion for transactions where each counterparty is a derivatives end-user that had commodity derivatives on its books at the end of each of the previous four calendar quarters with a total average of less than $250 million gross notional value. Once an end-user exceeds that threshold, it should be permitted one calendar quarter to prepare to operate without the exclusion or to get under the $250 million threshold. Such an approach will provide end-users with enough time and flexibility to make the relief provided by the proposed end-user exclusion from derivatives reporting meaningful.

To illustrate the concept, here is an example. Take an end-user with the following quarter-end gross notional values for the commodity derivatives on its books: Q1 2015-$250 million; Q2 2015-$230 million; Q3 2015-$260 million; Q4 2015-$250 million. This end-user would qualify for the exclusion since its total average is less than $250 million. If at the end of Q1 2016 the end-user has $290 million gross notional value of commodity derivatives on its

[19] This could be done in connection with a NYMEX CL futures position to hedge both directional price risk and the basis risk between the two prices.

books, the entity should be able to continue to qualify for the exclusion from reporting if it has less than $220 million gross notional value of commodity derivatives on its books at the end of Q2 2016. If it does not, it would lose the exclusion until its average gross notional value outstanding of commodity derivatives falls under $250 million.

E. The Compliance Timeline to Begin Reporting Derivatives Data Should Be Three Months After Derivatives Dealers Begin Reporting.

The Proposed TR Rule considers staggering compliance with reporting obligations such that derivatives dealers would begin reporting on a certain date followed by end-users beginning to report on a later date. The Working Group applauds the proposed staggered approach because it will allow recognized trade repositories to focus on onboarding a small set of market participants that will be obligated to report a vast majority of derivatives before focusing on end-users that will likely require more customer service resources to properly "on board" with trade repositories. This recommendation is a product of the Working Group's "lessons learned" from the implementation of reporting requirements in the United States where a short period of time between swap dealer and end-user compliance with regard to the reporting of commodity swaps resulted in the CFTC having to delay end-user compliance.

Given that trade reporting will likely be in effect for end-users in Manitoba, Ontario, and Quebec by the time the Proposed TR Rule becomes effective, the Working Group respectfully requests that the Participating Jurisdictions require end-users to begin reporting derivatives three months after derivatives dealers begin reporting.

III. COMMENTS OF THE WORKING GROUP ON OTHER TECHNICAL ISSUES.

A. Scope of Recordkeeping Requirements.

The text of the Proposed TR Rule requires the reporting counterparty to keep "transaction records," but the header of Section 36 of the Proposed TR Rule is "Records of data reported." As such, it is unclear whether the recordkeeping requirement in Section 36 of the Proposed TR Rule covers all data reported to a recognized trade repository or a subset of that data referred to in the rule as "transaction records."

The Working Group requests additional clarification on the scope of Section 36 of the Proposed TR Rule's recordkeeping requirement.

B. The Proposed TR Rule Should Provide Additional Guidance on How Data Will Be Made Available to Counterparties.

Under the Proposed TR Rule, recognized trade repositories must, among other things, provide each counterparty to a derivatives transaction access to all data relating to that transaction in a timely manner, regardless of whether the counterparties are participants of the recognized trade repository.[20] The Proposed TR Rule does not, however, discuss how a

[20] *See* Proposed TR Rule at Section 38(1).

recognized trade repository should go about providing access to non-participants whose trades are reported to such recognized trade repository.

The Working Group respectfully requests additional guidance on how trade repositories should be required to provide access to data to all counterparties.

C. The Exclusion of Derivatives Contracts Traded on an "Exchange" Should Recognize and Include a Broader Universe of Regulated Trading Facilities.

The Proposed Scope Rule provides that derivatives traded on certain exchanges that are recognized by a securities regulatory authority or a recognized foreign exchange are excluded and thus, not subject to the requirements under the Proposed TR Rule. Notably, an "exchange" in this context of the Proposed Scope Rule would not include any of the following:

- a "swap execution facility," as defined in the Commodity Exchange Act (United States);
- a "multilateral trading facility," as defined by the European Parliament in the Markets in Financial Instruments Directive (MiFID);
- an "organized trading facility," as defined in Directive 2014/65/EU Article 4(1)(23) of the European Parliament; or
- any entity organized in a foreign jurisdiction that is similar to an entity described above.

As such, derivative transactions on the above facilities would be subject to the Proposed TR Rule. Reporting of such derivatives transactions may be difficult, unless the trading facility can be used to satisfy the required reporting obligations in each relevant Canadian jurisdiction.[21]

The Working Group respectfully requests that the Participating Jurisdictions recognize additional trading facilities as an "exchange" or provide other necessary compliance relief, in order to avoid imposing unnecessary reporting obligations on Canadian entities, which may limit their access to financial markets abroad.

IV. CONCLUSION.

The Working Group appreciates this opportunity to provide comments on the Proposed Reporting Rules and respectfully requests that the comments set forth herein are considered as any final legislation or regulations are drafted.

If you have any questions, please contact the undersigned.

[21] Proposed Scope Rule at Sections 2(1)(g) and 2(2).

Respectfully submitted,
/s/ R. Michael Sweeney, Jr.
R. Michael Sweeney, Jr.
Alexander S. Holtan
Lillian A. Forero