

ALBERTA SECURITIES COMMISSION

STAFF NOTICE 91-703

Over-the Counter Derivatives

February 28, 2011

Introduction

The Commission proposes to regulate over-the-counter derivative transactions under the *Securities Act* (the Act) with the proposed repeal of Blanket Order 91-503 *Over the Counter Derivatives and Commodity Contracts* and the proposed enactment of Rule 91-505 *Over-the-Counter Derivatives* (collectively, the **Proposed Amendments**). The Commission is publishing the Proposed Amendments for comment with this Notice.

Substance and Purpose of the Proposed Amendments

In September 2009 the G-20 group of nations – which includes Canada – called for increased regulatory oversight in the over-the-counter derivatives markets with the following recommendation:

All standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest. OTC derivative contracts should be reported to trade repositories. Non-centrally cleared contracts should be subject to higher capital requirements.

The Proposed Amendments will restore the Commission's legal authority under the Act to implement the G-20 recommendations on regulating over-the-counter derivatives.

The Act categorizes an over-the-counter derivative as a futures contract in the legislated definition of a 'futures contract'. As such, an over-the-counter derivatives transaction is regulated as a securities transaction under the Act. This has two primary implications for an over-the-counter derivative transaction in Alberta, namely that the transaction is subject to both the registration and prospectus requirements in the Act. These requirements would apply but for the effect of Blanket Order 91-503 *Over the Counter Derivatives and Commodity Contracts* which declares most over-the-counter derivatives to not be a 'futures contract' pursuant to authority granted by section 10 of the Act. The proposed repeal of Blanket Order 91-503 *Over the Counter Derivatives and Commodity Contracts* would thus restore the Commission's legislated authority to regulate an over-the-counter derivatives transaction as a futures contract transaction under the Act.

The Commission proposes to enact Rule 91-505 *Over-the-Counter Derivatives* to alleviate difficulties associated with the fact that derivative transactions are generally not securities

transactions. Over-the-counter derivative transactions are generally confined to large institutional entities because of the amount of credit necessary to consummate the transaction. These institutional entities do not require the protections of securities legislation offered by the prospectus requirement. The Commission is also of the view that an over-the-counter derivative instrument that requires physical delivery of an underlying asset should not be regulated as a securities transaction under the Act. Rule 91-505 *Over-the-Counter Derivatives* reflects these views by exempting all over-the-counter derivative transactions from the prospectus requirement in the Act. This is also consistent with the fact that the Act does not submit exchange contract transactions to the prospectus requirement.

The Proposed Amendments are consistent with recommendations and legislative amendments in other jurisdictions. In November 2010 the Canadian Securities Administrators (CSA) issued its Consultation Paper 91-401 *Over-the-Counter Derivatives Regulation in Canada* wherein the CSA recommends that securities regulatory authorities obtain legal authority to implement the G-20 recommendations. Consultation Paper 91-401 is posted on the Commission website at www.albertasecurities.com. The Commission is considering disclosure and other requirements for certain over-the-counter derivative transactions, taking into account developments in other CSA jurisdictions.

The Commission intends to implement the Proposed Amendments with an effective date that is concurrent with the implementation of similar amendments in other CSA jurisdictions, and the Commission will provide reasonable notice in advance of such date.

How to provide your comments

If you would like to comment on the Proposed Amendments, you may submit written comments to:

David Linder, Q.C.
Executive Director
Alberta Securities Commission
Tel. (403) 297-4228
David.Linder@asc.ca

Comments must be received on or before April 29, 2011.

Alberta Securities Commission

Rule 91-505 *Over-the-Counter Derivatives*

Definitions

1. Terms defined in the *Securities Act*, R.S.A. 2000, c. S-4, National Instrument 14-101 *Definitions*, or National Instrument 31-103 *Registration Requirements and Exemptions* have the same meaning in this Rule.
2. In this Rule, “over-the-counter physical commodity contract” means a futures contract that
 - (a) is not an exchange contract,
 - (b) contains an obligation to make or take future delivery of a commodity other than cash or a currency, and
 - (c) does not allow for cash settlement in place of physical delivery.

Prospectus Exemption

3. The prospectus requirement does not apply to a distribution of a futures contract.

Registration Exemption

4. The dealer registration requirement does not apply in respect of a trade by a person or company in an over-the-counter physical commodity contract.

Effective Date

5. This Rule comes into force on _____.