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Via email: Christopher.Eccles@osfi-bsif.gc.ca

Christopher Eccles
Senior Pension Analyst
Office of the Superintendent of Financial Institutions (OSFI)
255 Albert Street
Ottawa, ON K1A 0H2

Dear Mr. Eccles:

Re: Draft Guideline for Derivatives Sound Practices for Federally Regulated Private Pension Plans

The Canadian Bar Association's Pensions and Benefits Law Section (CBA Section) is pleased to comment on OSFI's revised draft derivatives guideline, *Derivatives Sound Practices for Federally Regulated Private Pension Plans*, dated July 2017 (the Draft Guideline).

The CBA is a national association representing over 36,000 jurists, including lawyers, notaries, law teachers and students across Canada. We promote the rule of law, access to justice, effective law reform and provide expertise on how the law touches the lives of Canadians every day. The CBA Section contributes to national policy, reviews developing pensions and benefits legislation and promotes harmonization. It has members involved in pensions and benefits law across the country, including counsel who advise pension and benefit plan administrators, employers, unions, employees and employee groups, trust and insurance companies, pension and benefit consultants, and investment managers and advisors.

The CBA Section comments on Section 6.1, 7.1 and 9.1 of the Draft Guideline and also makes some general comments.

A. Section 6.1 of the Draft Guideline – *Independent Pricing and Value Measurements*

The *Independent Pricing and Value Measurements* subsection of Section 6.1 appears to require pension plan administrators to seek independent valuation inputs for derivatives. ISDA Agreements between pension plan administrators and counterparties typically provide for the counterparty to value the derivatives. The requirement for independent valuation inputs would unnecessarily increase transaction costs for pension plans, especially given that pension plan administrators are already subject to prudence requirements when making investments. We recommend that the

obligation to seek independent valuations be softened; for example, by suggesting that plan administrators consider seeking independent valuation inputs, rather than requiring them to.

The meaning of “independent” valuation could also be clarified – as currently drafted, it is not clear whether OSFI expects an independent valuation to be performed by a third party that is not a party to the ISDA Agreement, or whether an independent valuation could be performed by the pension plan administrator where it has the expertise to value derivatives, for example, where the administrator is a financial institution. We recommend that OSFI clarify that an independent valuation could be performed by a pension plan administrator where the administrator has the appropriate expertise, in order to minimize unnecessary transaction costs.

B. Subsection 7.1 of the Draft Guideline – *Netting Agreements*

Subsection 7.1 of the Draft Guideline, *Netting Agreements*, refers to both “close-out netting” and “payment netting” (see page 10, at the top of the page) in connection with the appropriate legal due diligence. We believe that, generally speaking, close-out netting is the most relevant concern with respect to counterparty credit risk. In our view, payment netting is more of an operational consideration. The focus of industry netting opinions, for example, is on the enforceability of close-out netting. It is not clear to us why a legal opinion on payment netting is advisable. The CBA Section recommends removing the reference to payment netting.

C. Section 9.1 of the Draft Guideline – *Regulatory Compliance*

At page 12 of the Draft Guideline, under Section 9.1, “*Regulatory Compliance*”, we believe that the word “reporting” in the second paragraph, second sentence is unnecessary and it should read “... may be subject to specific regulatory ~~reporting~~ requirements for registering, central clearing, risk mitigation and trade reporting if they transact in OTC derivatives”.

D. General Comments

The CBA Section has long advocated for an effective and efficient pension regulatory system and we believe that harmonization is key to facilitating that system. In the interests of harmonization, the CBA Section is concerned with any mandated differences and benefit rules that vary by jurisdiction. Many repurchase and securities lending arrangements are similar in structure and economic result to many of the financial instruments addressed by the Draft Guideline. In light of this, the CBA Section suggests that OSFI consider what application, if any, the principles articulated in the Draft Guideline may have with respect to those arrangements.

We appreciate the opportunity to share our views on the Draft Guideline. We trust that our comments will be of assistance and we would be pleased to provide any further clarifications.

Yours truly,

(original letter signed by Gillian Carter for Elizabeth Brown)

Elizabeth Brown
Chair, CBA Pensions and Benefits Law Section