



July 6, 2016

DELIVERED BY EMAIL TO: comment@ccmr-ocrmc.ca

To: The Cooperative Capital Markets Regulatory System

Dear Sir/Madam:

Revised Draft Capital Markets Stability Act

We are writing to provide comments on the Revised Draft Capital Markets Stability Act (“CMSA”) released for consultation on May 5, 2016.

The Canadian Life and Health Insurance Association (“CLHIA”) is a voluntary trade association that represents companies which together account for 99 per cent of Canada’s life and health insurance business. The industry, which provides employment to about 155,000 Canadians and has assets in Canada of over \$721 billion, protects about 28 million Canadians through products such as life insurance, annuities, registered retirement savings plans, disability insurance and supplementary health plans. It pays benefits of almost \$84 billion a year to Canadians and manages about two-thirds of Canada’s pension plans.

The CLHIA is supportive of the general direction of reducing systemic risk within the Canadian financial system. However, in the absence of clear examples of what products may represent systemic risk, it is difficult to comment with any degree of specificity on many of the concepts in the CMSA.

As compared to the first draft released in 2014, we have noted that some key improvements have been made to the CMSA. We agree with the shift away from entity-based regulation which would be duplicative and possibly result in uneven application of regulation. We support the direction of designating products as being systemically important and certain practices as systemically risky; however, more detail is required about the intended regulatory focus. Due to its very broad power to regulate systemic risk, products of life and health insurers may become subject to regulation under the CMSA, in addition to existing insurance regulation.

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Life insurance products are not systemically risky

Life and health insurance products provide Canadians with long-term financial protection and by their nature, these products are not systemically risky. Individual variable insurance contracts (“IVICs”) offered by life and health insurance companies are also not systemically risky because they include almost all equity capital and are subject to limits on the extent that they can use leverage or borrowing. The segregated funds in which IVICs invest are separate funds from an insurer’s general assets.

In addition, note that federally regulated life insurance companies are already subject to extensive prudential regulation by the Office of the Superintendent of Financial Institutions (“OSFI”) and provincially incorporated companies are subject to similar regulation by provincial regulators such as the Autorité des marchés financiers in Quebec.

Comments on the Draft Legislation

We have some specific comments on various aspects of the CMSA, as follows.

(i) Definition of systemic risk

The definition of systemic risk in section 3 has been made more focused by referencing a “material adverse effect on the Canadian economy”. We believe the definition would benefit from some further refinement by tying it more closely with the ability to designate benchmarks and practices as being systemically important and therefore subject to regulation under the CMSA. It would be helpful for the Capital Markets Regulatory Authority (“Authority”) to state what its regulatory focus is intended to be and to provide stakeholders the opportunity to comment on it.

(ii) Definition of investment fund

The definition of an investment fund may not be sufficiently clear: for example, it suggests that it may include segregated funds. In the French language version, the definition of “fonds d’investissement” includes “tout fonds distinct”. Literally translated, it would mean that investment funds include segregated funds. In the *Act Respecting Insurance (Quebec)*, the words “separate funds” are used to mean segregated funds. In French, the words “fonds distinct” should be changed.

In the English language version the term “separate fund” is used. A term such as “pooled fund” may be more correct.

(iii) Compliance reviews

The Authority is granted powers in section 28 to enter and use, copy or take away nearly any of a market participant’s records. We believe that these powers are overly broad. In a search of business premises, there are no process protections for market participants. If a compliance review does not proceed on a cooperative basis for some reason, it would seem appropriate to require that the powers of entry in subsection 28(7) be subject to court order or search warrant similar to those in subsection 30(1) whether the place being entered is a dwelling house or a business premises.

Regulatory coordination

Since the CMSA would apply in all jurisdictions, not just those jurisdictions participating in the new Cooperative Capital Markets Regulatory System (“CCMRS”), it is very important that the Authority work cooperatively with the non-participating jurisdictions. Consistent with this, it would seem logical to carry forward the existing Canadian Securities Administrators’ framework for discussion and development of policies to be adopted by all jurisdictions to help ensure harmonization in all jurisdictions.

It will create a lot of additional regulatory burden if market participants have to comply with inconsistent trade reporting requirements in different jurisdictions within Canada.

For federally regulated life insurers, it is very important that there be regulatory coordination with OSFI, particularly as insurers are subject to the OSFI guidelines related to derivatives management. It will also be important that requirements established by the Authority be consistent with the OSFI requirements.

We also note with interest the statement of the Canadian Council of Insurance Regulators (“CCIR”) in its May 2016 Segregated Funds Working Group Issues Paper confirming its position that the possibility that a participating jurisdiction in the CCMRS could choose to regulate segregated funds as a security could “lead to unnecessary duplication of regulation ... and would increase confusion among consumers.”

Principles-based regulation

We would like to encourage the Authority to adopt a model of principles-based regulation to the greatest extent possible. In such a model, the Authority would consult with market participants, issue guidance regarding products or practices considered systemically risky and monitor trends. Such a model allows for regulatory flexibility to quickly adapt to changes. Powers related to urgent orders should only be used in emergency circumstances.

The process for making regulations designating products or practices as systemically important should include a process for comment and consultation by market participants and should not allow for the arbitrary designation of a product as systemically risky. Such procedural requirements should be part of the legislative framework.

Operationalizing the CMSA

Before the CMSA moves forward, it will be important for the federal Department of Finance and the Authority to further explain the regulatory approach that would be taken to operationalize the CSMA and what specific impacts it could have on different industries. Certainly, the life and health insurance industry would be most interested in such discussions. We are of the view that more clarity as to the intent and purpose of the proposed Act is necessary before consultation can be concluded.

Should you have any questions regarding our comments, please contact me (416-359-2044 or fzinatelli@clhia.ca) or my colleague James Wood (416-359-2025 or JWood@clhia.ca).

Yours very truly,

Frank Zinatelli

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