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| <input type="checkbox"/> | Trading – Interest Rate Derivatives | <input type="checkbox"/> | Back-office - Options |
| <input type="checkbox"/> | Trading – Equity and Index Derivatives | <input type="checkbox"/> | Technology |
| <input type="checkbox"/> | Back-office – Futures | <input checked="" type="checkbox"/> | Regulation |

CIRCULAR
February 1, 2007

**MARGIN AND CAPITAL REQUIREMENTS FOR OPTIONS,
FUTURES CONTRACTS AND OTHER DERIVATIVE INSTRUMENTS –
RULE NINE OF BOURSE DE MONTRÉAL INC.**

**AMENDMENTS TO ARTICLES 9001, 9003, 9103, 9105, 9106, 9108, 9109,
9203, 9205, 9206, 9208, 9209, 9301 AND 9401**

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved amendments to articles 9001, 9003, 9103, 9105, 9106, 9108, 9109, 9203, 9205, 9206, 9208, 9209, 9301 and 9401 of Rule Nine of the Bourse, which deal with margin and capital requirements applicable to options, futures contracts and other derivative instruments. These amendments are effective immediately.

The purpose of these amendments is to harmonize the language of some provisions of Rule Nine of the Bourse relating to margin and capital requirements applicable to options, futures contracts and other derivative instruments with the wording of Regulations 100.9 and 100.10 of the Investment Dealers Association of Canada (IDA). Such harmonization of the language used will eliminate any risk of differing interpretation of the applicable regulatory requirements. The amendments also add to article 9001 of the Rules a definition of the term “participation unit”.

For further information, please contact Mr. Vito Racanelli, Financial Analyst, Regulatory Division, at 514 871-4949, extension 339, or by e-mail at vracanelli@m-x.ca.

Joëlle Saint-Arnault
Vice-President, Legal Affairs and Secretary

Circular no.: 018-2007
Amendment no.: 001-2007

**RULE NINE
MARGIN AND CAPITAL REQUIREMENTS
FOR OPTIONS, FUTURES CONTRACTS AND
OTHER DERIVATIVE INSTRUMENTS**

**Section 9001 – 9100
General Provisions**

9001 Definitions
(01.01.05, 01.02.07)

For the purpose of the present Rule:

(...)

k) “**participation unit**” means a unit of beneficial interest in the assets of a fund established under a trust agreement, the underlying asset of which are equities or other securities;

(...)

9003 Inter-Commodity Combinations
(01.01.05, 01.02.07)

Unless otherwise specified, offsets are not permitted for positions in client accounts or approved participant accounts involving derivative instruments based on two different underlying interests.

Section 9101 – 9200
Margin Requirements on Equity-Related Derivatives

9103 Short Option Positions
(01.01.05, 01.02.07)

- a) The minimum margin requirement which must be maintained in respect of an option carried short in a client account must be:
 - i) 100% of the market value of the option; plus
 - ii) a percentage of the market value of the underlying interest determined using the following percentages:
 - A) for equity options or equity participation unit options, the margin rate applicable to the underlying interest;
 - B) for index options or index participation unit options, the published floating margin rate for the index or index participation unit;

minus

 - iii) any out-of-the-money amount associated with the option;
- b) paragraph a) notwithstanding, the minimum margin requirement which must be maintained and carried in a client account trading in options must not be less than:
 - i) 100% of the market value of the option; plus
 - ii) an additional requirement determined by multiplying:
 - A) in the case of a short call option, the market value of the underlying interest; or
 - B) in the case of a short put option, the aggregate exercise value of the option;

by one of the following percentages:

 - C) for equity options or equity participation unit options, 5%; or
 - D) for index options or index participation unit options, 2%.

9105 Option Spreads and Combinations

(01.01.05, 01.02.07)

a) Call spreads and put spreads

Where a client account contains one of the following spread pairings:

- long call option and short call option; or
- long put option and short put option;

and the short option expires on or before the date of expiration of the long option, the minimum margin required for the spread pairing must be the lesser of:

- i) the margin required on the short option pursuant to article 9103; or
- ii) the spread loss amount, if any, that would result if both options were exercised.

(...)

9106 Option and Security Combinations

(01.01.05, 01.02.07)

a) Short call – long underlying (or convertible) combination

Where, in the case of equity or equity participation unit options, a call option is carried short in a client's account and the account is also long an equivalent position in the underlying interest or, in the case of equity options in a security readily convertible or exchangeable (without restrictions other than the payment of consideration and within a reasonable time provided such time must be prior to the expiration of the call option) into the underlying interest, or in the case of equity participation unit options in securities readily exchangeable into the underlying interest, the minimum margin required must be the sum of:

- i) the lesser of
 - A) the normal margin required on the underlying interest; and
 - B) any excess of the aggregate exercise value of the call options over the normal loan value of the underlying interest;

and

- ii) where a convertible security or exchangeable security is held, any excess of the market value of the convertible or exchangeable security over the market value of the equivalent number of underlying securities.

In the case of exchangeable or convertible securities, the right to exchange or convert the long security must not expire prior to the expiration date of the short call option. If the expiration of the right to exchange or convert is accelerated (whether by reason of redemption or otherwise), then such short call option must be considered uncovered after the date on which such right to exchange or convert expires.

b) Short put – short underlying combination

Where, in the case of equity or equity participation unit options, a put option is carried short in a client's account and the account is also short an equivalent position in the underlying interest, the minimum margin required must be the lesser of:

- i) the normal margin required on the underlying interest; and
- ii) any excess of the normal credit required on the underlying interest over the aggregate exercise value of the put option.

(...)

9108 Index Option and Index Participation Unit Option Spread Combinations
(01.01.05, 01.02.07)

a) Call spread combinations and put spread combinations

Where a client account contains one of the following spread combinations:

- long index call option and short index participation unit call option; or
- long index put option and short index participation unit put option; or
- long index participation unit call option and short index call option; or
- long index participation unit put option and short index put option;

and the short option expires on or before the date of expiration of the long option, the minimum margin required for the spread combination must be the lesser of:

- i) the margin required on the short option pursuant to article 9103; and
- ii) the greater of:
 - A) the loss amount, if any, that would result if both options were exercised; and
 - B) the published tracking error margin rate for a spread between the index and the related index participation units, multiplied by the market value of the underlying index participation units.

9109 Index Option Combinations with Qualifying Baskets of Index Securities and Index Participation Units
(01.01.05, 01.02.07)

a) Short call option combinations with long qualifying baskets of index securities or long index participation units

Where a client account contains one of the following option related combinations:

- short index call options and long an equivalent number of qualifying baskets of index securities;
or
- short index call options and long an equivalent number of index participation units (note: subject to tracking error minimum margin); or
- short index participation unit call options and long an equivalent number of qualifying baskets of index securities (note: subject to tracking error minimum margin); or
- short index participation unit call options and long an equivalent number of index participation units;

the minimum margin required must be the greater of:

- i) the lesser of
 - A) the normal margin required on the qualifying basket of index securities (or index participation units); and
 - B) any excess of the aggregate exercise value of the call options over the normal loan value of the qualifying basket of index securities (or index participation units);

and

- ii) where applicable, the published tracking error margin rate for a spread between the index and the related index participation units, multiplied by the market value of the underlying index participation units.

b) Short put option combinations with short qualifying baskets of index securities or short index participation units

Where a client account contains one of the following option related combinations:

- short index put options and short an equivalent number of qualifying baskets of index securities;
or

- short index put options and short an equivalent number of index participation units (note: subject to tracking error minimum margin); or
- short index participation unit put options and short an equivalent number of qualifying baskets of index securities (note: subject to tracking error minimum margin); or
- short index participation unit put options and short an equivalent number of index participation units;

the minimum margin required must be the greater of:

i) the lesser of

- A) the normal margin required on the qualifying basket of index securities (or index participation units); and
- B) any excess of the normal credit required on the underlying interest qualifying basket of index securities (or index participation units) over the aggregate exercise value of the put option;

and

ii) where applicable, the published tracking error margin rate for a spread between the index and the related index participation units, multiplied by the market value of the underlying index participation units.

(...)

9203 Short Option Positions
(01.01.05, 01.02.07)

The minimum capital required which must be maintained in respect of an option carried short in an approved participant account must be:

- i) A) for equity options or equity participation unit options, the market value of the equivalent number of equity securities or participation units multiplied by the underlying interest margin rate; or
- B) for index participation unit options, the market value of the equivalent number of index participation units multiplied by the floating margin rate; or
- C) for index options, the aggregate current value of the index, multiplied by the floating margin rate;

minus

- ii) any out-of-the-money amount associated with the option.

9205 Option Spreads and Combinations
(01.01.05, 01.02.07)

a) Call spreads and put spreads

Where an approved participant account contains one of the following spread pairings:

- long call option and short call option; or
- long put option and short put option;

the minimum capital required must be the lesser of:

- i) the capital required on the short option pursuant to article 9203; or
- ii) the spread loss amount, if any, that would result if both options were exercised.

(...)

c) Long call – long put spreads

Where a call option is carried long for an approved participant's account and the account is also long a put option on the same number of units of trading on the same underlying interest, the minimum capital required must be the lesser of:

- i) the sum of:
 - A) the capital required for the call option; and

B) the capital required for the put option;

and

ii) the sum of:

A) 100% of the market value of the call option; plus

B) 100% of the market value of the put option; minus

C) the amount by which the aggregate exercise value of the put option exceeds the aggregate exercise value of the call option.

(...)

9206 Options and Security Combinations

(01.01.05, 01.02.07)

a) Short call – long underlying (or convertible) combination

Where, in the case of equity or equity participation unit options, a call option is carried short in an approved participant's account and the account is also long an equivalent position in the underlying interest or in the case of equity options in a security readily convertible or exchangeable (without restrictions other than the payment of consideration and within a reasonable time provided such time must be prior to the expiration of the call option) into the underlying interest, or in the case of equity participation unit options in securities readily exchangeable into the underlying interest, the minimum capital required must be the sum of:

i) the lesser of

A) the normal capital required on the underlying interest; and

B) any excess of the aggregate exercise value of the call options over the normal loan value of the underlying interest;

and

ii) where a convertible security or exchangeable security is held, any excess of the market value of the convertible or exchangeable security over the market value of the equivalent number of underlying securities.

The market value of the short call option may be used to reduce the capital required on the long security, but cannot reduce the capital required to less than zero.

b) Short put – short underlying combination

Where, in the case of equity or equity participation unit options, a put option is carried short in an approved participant's account and the account is also short an equivalent position in the underlying interest, the minimum capital required must be the lesser of:

- i) the normal capital required on the underlying interest; and
- ii) any excess of the normal capital required on the underlying interest over the in-the-money value, if any, of the put option.

The market value of the short put option may be used to reduce the capital required on the short security, but cannot reduce the capital required to less than zero.

(...)

f) Reconversion or short tripo combination

Where, in the case of equity or equity participation unit options, a position in an underlying interest is carried short in an approved participant's account and the account is also long an equivalent position in call options and short an equivalent position in put options, the minimum capital required must be:

- i) 100% of the market value of the long call options; minus
- ii) 100% of the market value of the short put options; plus
- iii) the difference, plus or minus, between the aggregate exercise value of the long call options and the market value of the underlying interest, where the aggregate exercise value used in the calculation cannot be greater than the aggregate exercise value of the put options.

9208 Index Options and Index Participation Unit Option Spread Combinations
(01.01.05, 01.02.07)

a) Call spread combinations and put spread combinations

Where an approved participant account contains one of the following spread combinations:

- long index call option and short index participation unit call option; or
- long index participation unit call option and short index call option; or
- long index put option and short index participation unit put option; or
- long index participation unit put option and short index put option;

and the short option expires on or before the date of expiration of the long option, the minimum capital required must be the lesser of:

- i) the capital required on the short option pursuant to article 9203; and
- ii) the greater of:
 - A) the spread loss amount, if any, that would result if both options were exercised; and
 - B) the published tracking error margin rate for a spread between the index and the related participation units, multiplied by the market value of the underlying participation units.

(...)

9209 Index Option Combinations with Qualifying Baskets of Index Securities and Index Participation Units
(01.01.05, 01.02.07)

a) Short call option combinations with long qualifying baskets of index securities or long index participation units

Where an approved participant account contains one of the following option related combinations:

- short index call options and long an equivalent number of qualifying baskets of index securities;
or
- short index call options and long an equivalent number of index participation units (note: subject to tracking error minimum margin); or
- short index participation unit call options and long an equivalent number of qualifying baskets of index securities (note: subject to tracking error minimum margin); or

- short index participation unit call options and long an equivalent number of index participation units;

the minimum capital required must be the greater of:

i) the lesser of

- A) the normal capital required on the qualifying basket of index securities (or index participation units); and
- B) any excess of the aggregate exercise value of the call options over the normal loan value of the qualifying basket (or participation units);

and

ii) where applicable, the published tracking error margin rate for a spread between the index and the related index participation units, multiplied by the market value of the underlying index participation units.

b) Short put option combinations with short qualifying index baskets or short index participation units

Where an approved participant account contains one of the following option related combinations:

- short index put options and short an equivalent number of qualifying baskets of index securities; or
- short index put options and short an equivalent number of index participation units (note: subject to tracking error minimum margin); or
- short index participation unit put options and short an equivalent number of qualifying baskets of index securities (note: subject to tracking error minimum margin); or
- short index participation unit put options and short an equivalent number of index participation units;

the minimum capital required must be the greater of:

i) the lesser of

- A) the normal capital required on the qualifying basket of index securities (or index participation units); and
- B) any excess of the normal capital required on the underlying interest over the in-the-money value, if any, of the put option;

and

- ii) where applicable, the published tracking error margin rate for a spread between the index and the related index participation units, multiplied by the market value of the underlying index participation units.

(...)

Section 9301 – 9400
Margin Requirements on Interest Rate Related Derivatives

9301 Exchange Traded Options - General
(01.01.05, 01.02.07)

- a) The Bourse shall establish margin requirements applicable to options positions held by clients and no approved participant shall effect an option transaction or carry an account for a client without proper and adequate margin, which must be obtained as promptly as possible and maintained in conformity with the provisions of this section;
- b) all opening selling transactions and resulting short positions must be carried in a margin account;
- c) each option must be margined separately and any difference between the market price of the underlying interest and the exercise price of the option must be considered to be of value only in providing the amount of margin required on that particular option;
- d) where a client account holds both CDCC options and OCC options that have the same underlying interest, the OCC options may be considered to be options for the purposes of the calculation of the margin requirements for the account under the provisions of this section;
- e) from time to time the Bourse may impose special margin requirements with respect to particular options or particular positions in options.

Section 9401 - 9500
Capital Requirements on Interest Rate Related Derivatives

9401 Exchange Traded Options – General
(01.01.05, 01.02.07)

- a) With respect to an approved participant account or market maker account, or of a restricted trading permit holder account for which an approved participant (or a clearing firm) has issued a letter of authorization or of a sponsor account, the Bourse has established certain charges against capital;
- b) in the treatment of spreads, the long position may expire before the short position;
- c) for any short position carried for a client or non-client account where the account has not provided required margin, any shortfall will be charged against the approved participant's capital;
- d) where an approved participant account holds both CDCC options and OCC options that have the same underlying interest, the OCC options may be considered to be options for the purposes of the calculation of the capital requirements for the account under the provisions of this section;
- e) from time to time the Bourse may impose special capital requirements with respect to particular options or particular positions in options;
- f) in the pairing described in articles 9405, 9406 and 9424, options of different classes for which the underlying bonds have the same margin rate may be paired together provided that:
 - i) the exercise price of the option for which the market value of the underlying bond is the lowest must be increased by the difference between the market value of the underlying bonds; and
 - ii) to the capital required pursuant to articles 9405, 9406 and 9424 must be added an amount equal to the margin that would be required on the net bond position which would result if both options were exercised.