

MONTREAL EXCHANGE - REGULATORY DIVISION

Newsletter

The Montreal Exchange Inc. (the “Bourse”) is recognized by the Autorité des marchés financiers (the “Autorité”) as an exchange and a self-regulatory organization. The Regulatory Division (the “Division”) is a separate business unit of the Bourse responsible for carrying out its regulatory functions and operations. The Division consists of three units: examinations, market analyses and investigations, and regulatory and disciplinary affairs.

The Division publishes a bi-annual newsletter to share information of a general nature on regulatory activities, and takes advantage of this opportunity to share observed best practices in regulatory compliance.

This newsletter covers the period from July 1 to December 31, 2018 and, for certain sections, provides a summary of 2018.

Enjoy!

Topics

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Publications of the Division in 2018

Participant Portal

Profile of approved participants and persons

- Approved participants
- Approved persons

Regulatory activities

- Examinations
- Market analysis and investigations
- Disciplinary proceedings
- Fines for minor violations
- Imposition of late filing fees

Observed best practices in applications for approval as an approved person

Coming events organized by the Division

Events organized by the Division

- A meeting was held in Toronto on October 10 and a phone meeting was held on December 11 with the Division's Regulatory User Group.
- On November 26, the Division held a Compliance Forum at the Canadian Annual Derivatives Conference (CADC).
- The Division had an information booth at CADC where, among other things, participants could learn about the Participant Portal, which is planned to be launched in the first quarter of 2019.

Publications of the Division in 2018

- **Participant admissions and resignations** (circulars [018-18](#), [019-18](#), [039-18](#), [040-18](#), [106-18](#), [107-18](#), [174-18](#), [203-18](#))
- **Name change of an approved participant** (circular [113-18](#))
- **Process for approval as an approved person** (circulars [119-18](#), [154-18](#), [160-18](#), [179-18](#))
- **Position limits** (circulars [005-18](#), [023-18](#), [030-18](#), [035-18](#), [037-18](#), [038-18](#), [049-18](#), [052-18](#), [060-18](#), [091-18](#), [101-18](#), [102-18](#), [115-18](#), [137-18](#), [151-18](#), [157-18](#), [158-18](#), [163-18](#), [177-18](#), [192-18](#), [193-18](#), [194-18](#))
- **LOPR and the Gatekeeper portal**
 - Reminder concerning LOPR reportable dates (circular [036-18](#))
 - Update to the password policy for the large open position reporting (LOPR) portal and the Gatekeeper portal (circular [095-18](#))
 - Enhancement to the large open position reporting (LOPR) tool (circular [117-18](#))
- **Changes to rules and procedures**
 - Request for comments concerning a proposal to amend article 4002 of the Rules of the Bourse (3.105 since January 1, 2019) initiated by the Division (circular [072-18](#))
 - Self-certification of amendments to the rules and procedures of the Bourse to expand the definition of an approved person (circular [111-18](#))
 - Self-certification of amendments to article 4002 of the Rules of the Bourse (3.105 since January 1, 2019) (circular [120-18](#))
- **Frequently asked questions**
 - Identification of orders (article 6.115, formerly article 6376) (circular [048-18](#))
 - Self-matching of orders and wash trading (article 7.5, formerly article 6306) (circular [176-18](#))
- **Disciplinary decisions** (circulars [011-18](#) and [099-18](#))
- **Other**
 - Call for applications from interested and qualified persons in order to fill one seat as an independent member of the Special Committee (circular [021-18](#))
 - Mission, vision, compliance priorities and 2018 Regulatory Division initiatives (circular [027-18](#))
 - New mandatory forms to access the Bourse's trading system (circular [118-18](#))
 - Comparative analysis by the Regulatory Division of market data in the context of the extension of trading hours (circular [135-18](#))
 - Publication of newsletters from the Regulatory Division (circulars [046-18](#) and [141-18](#))

Participant Portal

The Division announced the launch of the Participant Portal (the “Portal”) in the first quarter of 2019. The Portal will be a secure and user-friendly single point of contact for participants. It will facilitate access to regulatory documents as well as the submission of applications, reports and notices to the Division.

In the last quarter of 2018, the Division completed the following activities related to the portal:

- Implementation of a system for the secure transfer of documents.
- Launch of a pilot project with volunteer participants for the initial functionalities available on the Portal. These functionalities are for:
 - Approved persons;
 - MX-ID;
 - Notices of non-compliance (Gatekeeper); and
 - Corrections to the identification of orders.

In 2019, a series of improvements will be made to these initial functionalities.

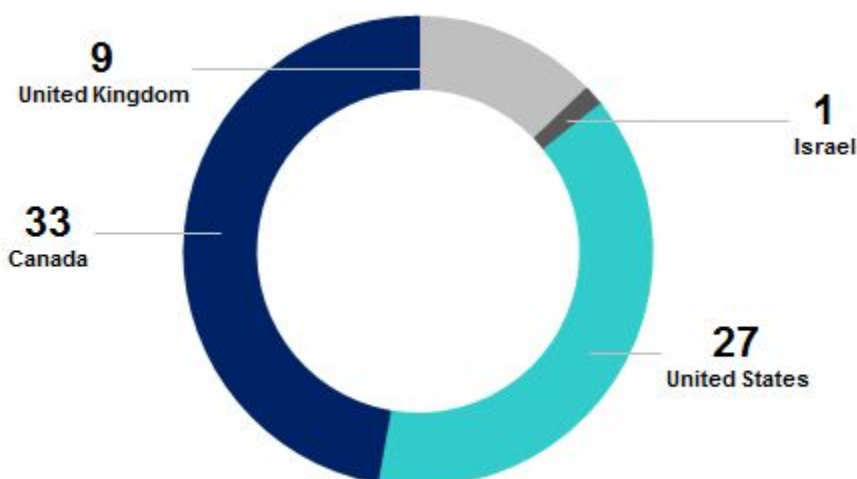
Profile of approved participants and persons

Approved participants

As at December 31, 2018, following admissions and resignations of participants, the Bourse had a total of 70 approved participants, distributed geographically as follows:

Figure 1

Approved participants as at December 31, 2018

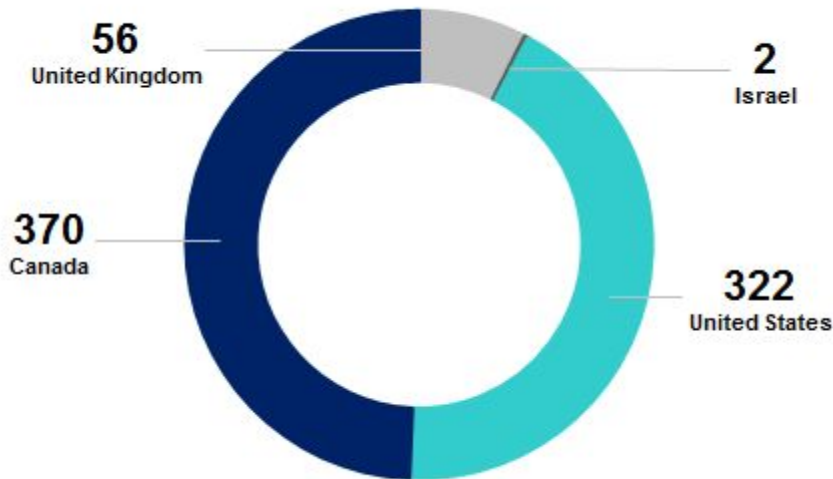


Approved persons

As at July 1, 2018, the Bourse had 756 approved persons. In the third and fourth quarters of 2018, the Division processed 55 new applications as approved persons as well as 61 termination notices.¹ As at December 31, 2018 the Bourse had 750 approved persons, distributed geographically as follows:

Figure 2

Approved persons as at December 31, 2018



Regulatory activities

Examinations

The Examinations unit manages examinations of the derivatives trading of the approved participants of the Bourse. The purpose of these examinations is to validate the compliance of approved participants of the Bourse with its Rules.

From July 1 to December 31, 2018, the Division performed 18 examinations leading to observations. Recurring observations include:

- Inadequate supervisory systems and incomplete policy and procedure manuals (see [article 3.100](#));
- Incorrect order account type markers (see [article 6.115](#));
- Failure to perform an annual evaluation of clients with direct electronic access (see [article 3.5](#)); and
- Failure to obtain approval from the Bourse as an approved person before granting access to the Electronic Trading System to one or more employees (see [article 3.400](#)).

In addition, during the period the Examinations unit issued management advice concerning exchanges for related products and related to [Regulation 23-103 respecting Electronic Trading and Direct Electronic Access to Marketplaces](#). Management advice is a recommendation formulated by the Examinations unit to a participant that reflects best practices observed concerning a regulatory issue.

¹ Uniform Termination Notice (UTN)

During the period from July 1 to December 31, 2018, the Division made a total of eighteen examinations leading to findings. In 2018, the Division performed a total of thirty-six examinations, or nine more than in 2017.

Review of the examination program

The Division's Examinations unit, with the assistance of an external consulting firm specialized in risk management, improved the method used to assess the risks of its participants to better align them with best practices.

A participant's risk rating is established on the basis of factors such as inherent risk, the design of controls, and residual risk. Risk ratings are calculated using a dynamic analysis process.

In addition, changes have been made to the questionnaire that a participant must complete when initial documentation is requested. Questions have been added to better reflect today's derivatives market and obtain more detailed information on certain subjects.

Market analysis and investigations

The Market Analysis unit performs market surveillance to detect potential breaches of regulations and monitors insider trading activities on the options market of the Bourse. The Market Analysis unit also reviews trading on the Bourse to determine whether participants are complying with trading rules and principles, and whether these trades involve abusive or manipulative trading practices.

An increase of 16.08% was observed in the average daily trading volume compared to the same period of 2017, for an average daily volume for the period of January to December 2018 of 446 984 contracts, compared to 385 070 contracts for the same period in 2017. In the second half of the year, from July 1 to December 31, 2018, the Division monitored over 8 665 660 trades executed on the Bourse.

The Market Analysis unit is also responsible for conducting preliminary reviews of all complaints received from various sources. The Division received six complaints in the period from July 1 to December 31, 2018, three of which were from clients.

In 2018, the Division received twelve complaints, eight of which were from clients.

The Investigations unit may open an investigation when a potential regulatory violation has been detected during an examination or following a market analysis.

From July 1 to December 31, 2018, the Division opened seven investigations, in particular concerning access to the trading system of the Bourse by employees of participants when those employees were not approved persons, and the supervision of the activities of clients with direct electronic access. During the same period, the Division completed two investigations.

In 2018, the Division opened ten investigations concerning electronic trading (Regulation 23-103), the supervision of clients with direct electronic access and the manipulation of closing prices.

Disciplinary proceedings

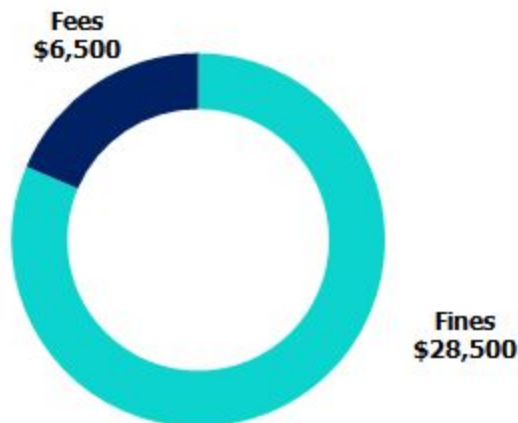
Disciplinary proceedings may be initiated when, following an investigation, the Division concludes that there has been an offence under the Rules of the Bourse or to regulation (for example, [Regulation 23-103 respecting Electronic Trading and Direct Electronic Access to Marketplaces](#)).

Disciplinary decisions

In the period from July 1 to December 31, 2018, no disciplinary decisions were rendered. However, in 2018, offences to the Rules of the Bourse that were subject to disciplinary decisions concerned: (1) the failure of an approved participant in its obligation to record and/or keep the recorded telephone conversations related to trading in securities or derivative instruments listed on the Bourse ([Circular 011-18](#)); and (2) the failure of an approved participant to report immediately to the Vice-President of the Regulatory Division of the Bourse that its account exceeded the position limit and failure in its obligation to establish and maintain a system to supervise the activities of each employee that is reasonably designed to achieve compliance with the Rules and Policies of the Bourse ([Circular 099-18](#)).

Figure 3

Fees and fines imposed as part of disciplinary matters in 2018



Fines for minor violations

In 2018, the Division did not use the process for imposing fines for minor violations.

Two disciplinary matters were settled in 2018. For these disciplinary matters, the fines paid by the participants totalled \$28,500, plus \$6,500 for the reimbursement of costs. All these amounts were collected by the Division and paid into the Fine Fund.

Imposition of late fees

The following table provides detailed information on all the fees imposed by the Division in the third and fourth quarters of 2018 for the late filing of documents.

Figure 4

Late Fees July 1 to December 31, 2018	Occurrences	Participants	Total amount imposed
Termination notice submitted more than 10 days after the termination date ²	4	4	\$4,000
Late reporting of corporate amendments	0	0	\$0
Report pertaining to the accumulation of positions for derivative instruments (LOPR) ³	22	17	\$39,500
Bi-monthly report on options over-the-counter options (Rule Nine) ⁴	3	2	\$8,200
Information or document required by the Division	0	0	\$0

Observed best practices in applications for approval as an approved person

To access the electronic trading system of the Bourse, the employees of an approved participant must be approved in accordance with Part 3 of the Rules of the Bourse. An application for approval must be filed with the Division as set forth in [article 3.400](#) of the Rules of the Bourse. (See also [Guidelines on the approval process for approved persons](#)),

As part of its analysis of approval applications, the Division has observed the following best practices:

- All the required sections and fields of the forms have been completed, and all the documents required in support of the application have been attached, which helps avoid delays in processing the application;
- The supporting documents satisfy the criteria, and are generally:
 - For an employee who is not a citizen in the country of employment, a copy of a valid document clearly indicating that he is eligible to work there. Where applicable, a written note from the designated representative, director or other representative (e.g. the Chief Compliance Officer) of the approved participant confirming that the applicant is authorized to work in his country of residence.

² One Canadian participant and three foreign participants

³ Nine Canadian participants and eight foreign participants

⁴ Two Canadian participants

- If the application form or other attachment has been signed by someone other than the designated representative, a copy of the corporate resolution authorizing the signatory to sign such an application on behalf of the approved participant and, or when applicable, on behalf of the affiliated corporation or subsidiary of the approved participant.
- Proof of the applicant's registration with a regulatory authority in the jurisdiction of his residence, or a document certifying an exemption in force at the time of filing the application for approval for the desired activity on the Bourse. In the absence of such a document certifying an exemption, a legal opinion or written note from the legal department or Chief Compliance Officer of the approved participant, confirming that the applicant is not subject to registration in the relevant jurisdiction, citing the applicable rules.
- The certificate confirming that the applicant has completed the training required by the Bourse must be signed by the applicant after having bought the course and read its contents.

Coming events organized by the Division

The Division's Regulatory User Group meetings

- March 1, 2019, meeting in Montréal;
- May 29, 2019, conference call meeting;
- October 2, 2019, meeting in Toronto; and
- December 11, 2019, conference call meeting.

“Derivatives Exchange / Parlons dérivés,” organized by the Division

- June 4, 2019 in Toronto and June 11, 2019 in Montréal (in French)

For more information:

REGULATORY DIVISION

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