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

**CIRCULAR**  
April 7, 2004

## **REQUEST FOR COMMENTS**

### **ACCEPTABLE SECURITIES LOCATIONS**

#### **AMENDMENTS TO THE GENERAL NOTES AND DEFINITIONS OF THE "JOINT REGULATORY FINANCIAL QUESTIONNAIRE AND REPORT" – POLICY C-3 OF THE BOURSE**

##### **Summary**

The Special Committee – Regulatory Division of Bourse de Montréal Inc. (the "Bourse") has approved amendments to the General Notes and Definitions of the "Joint Regulatory Financial Questionnaire and Report" – Policy C-3 of the Bourse, which deal with the definition of acceptable securities locations. The purpose of the proposed amendments is to require that a written custodial agreement be entered into when a bank or a trust company which acts as transfer agent also offers custody services in order to be considered as an acceptable securities location.

##### **Process for Changes to the Rules**

Bourse de Montréal Inc. is recognized as a self-regulatory organization (SRO) by the Autorité des marchés financiers ("the Autorité"). In accordance with this recognition, the Bourse carries on activities as an exchange and as a SRO in Québec. In its SRO capacity, the Bourse assumes market regulation and broker-dealers regulation responsibilities. The broker-dealers regulated by the Bourse are its approved participants. The responsibility for regulating the market and the approved participants of the Bourse comes under the Regulatory Division of the Bourse ("the Division"). The Division carries on its activities as a distinct business unit separate from the other activities of the Bourse.

Circular no.: 040-2004

The Division is under the authority of a Special Committee appointed by the Board of Directors of the Bourse. The Board of Directors of the Bourse has delegated to the Special Committee – Regulatory Division its powers to approve or amend some aspects of the Rules and Policies of the Bourse governing approved participants, among which, the Rules and Policies relating to admission as approved participant, approval of persons, disciplinary matters, management of client accounts and operations. These changes are submitted to the Autorité for approval.

Comments on the proposed amendments to the definition of acceptable securities locations contained in the General Notes and Definitions of Policy C-3 of the Bourse must be submitted within 30 days following the date of publication of the present notice in the bulletin of the Autorité. Please submit your comments to:

*Ms. Joëlle Saint-Arnault  
Vice-President, Legal Affairs and Secretary  
Bourse de Montréal Inc.  
Tour de la Bourse  
P.O. Box 61, 800 Victoria Square  
Montréal, Quebec H4Z 1A9  
E-mail: [legal@m-x.ca](mailto:legal@m-x.ca)*

A copy of these comments shall also be forwarded to the Autorité to:

*Ms. Anne-Marie Beaudoin  
Director – Secretariat of L'Autorité  
Autorité des marchés financiers  
800 Victoria Square, 22<sup>nd</sup> Floor  
P.O. Box 246, Tour de la Bourse  
Montréal (Quebec) H4Z 1G3  
E-mail: [consultation-en-cours@lautorite.qc.ca](mailto:consultation-en-cours@lautorite.qc.ca)*

## **Appendices**

For your information, you will find in appendices an analysis document of the proposed rule amendments as well as the proposed regulatory text. The implementation date of the proposed amendments will be determined, if applicable, with the other Canadian self-regulatory organizations following approval by the "Autorité des marchés financiers".



### ACCEPTABLE SECURITIES LOCATIONS

#### – AMENDMENTS TO THE GENERAL NOTES AND DEFINITIONS OF THE “JOINT REGULATORY FINANCIAL QUESTIONNAIRE AND REPORT” – POLICY C-3 OF BOURSE DE MONTREAL INC.

#### I DETAILED ANALYSIS

##### A) Current Rules

Under the current rules of Bourse de Montreal Inc. (the “Bourse”), “acceptable securities locations” means those entities considered suitable to hold securities on behalf of an approved participant, for both inventory and client positions, without capital penalty. The locations of these entities must meet the requirements outlined in the segregation rules of the Bourse. These requirements include, among other things, the obligation to have a written custody agreement that includes the following provisions, as described in article 7511 of the Rules of the Bourse:

- no use or disposition of the securities must be made without the prior written consent of the approved participant;
- certificates representing the securities can be delivered to the approved participant promptly on demand or, where certificates are not available and the securities are represented by book entry at the location, the securities can be transferred either from the location or to another person at the location promptly on demand; and
- the securities are held in segregation or safekeeping for the approved participant or

its clients free and clear of any charge, lien, claim or encumbrance of any kind in favour of the depository or institution holding such securities.

Paragraph d) of the General Notes and Definitions of Policy C-3 of the Bourse enumerate the entities that are considered as “acceptable securities locations”.

##### B) The Issue

Banks and trust companies classified as acceptable counterparties may be considered as acceptable securities locations with respect to securities for which they act as transfer agent. In such case, as specified in point 4 of paragraph d) of the General Notes and Definitions of Policy C-3 of the Bourse, it is not required to have a written custody agreement. Originally, this exemption was intended particularly for situations where securities are sent to the transfer agent for re-registration and not for the general holding of those securities. However, an approved participant could refer to this exemption to let a bank or a trust company hold securities on its behalf without a written custody agreement by stating that the bank or trust company acts also as transfer agent. To avoid this situation it is proposed to modify the wording in point 4 of paragraph d) of the General Notes and Definitions of Policy C-3 of the Bourse to read as follows:

4. *Banks and Trust Companies otherwise classified as Acceptable Counterparties – with respect to securities for which they act as transfer agent and for which custody services are not being provided (in such case, a written custody agreement is not required).*

##### C) Objective and Effect of Proposed Rules

The objective of the proposed amendments to paragraph d) of the General Notes and Definitions of Policy C-3 of the Bourse is to require a written custody agreement when a

bank or a trust company acts as transfer agent and offers custody services for the bank or the trust company be considered as an acceptable securities location. Consequently, the exemption of having a written custody agreement will only apply in the case where the bank or the trust company acts solely as transfer agent without providing custody services.

### **D) Public Interest Objective**

The objective of the proposed amendments is to clarify in which circumstance a written custody agreement is not required, i.e. when the bank or trust company acts solely as transfer agent. Consequently, the proposed amendments are considered to be in the public interest.

## **II COMMENTARIES**

### **A) Effectiveness**

The proposed amendments will clarify the situations where a written custody agreement is not required so that banks and trust companies acting as transfer agents can be considered as acceptable securities locations.

### **B) Process**

The first step of the approval process for the regulatory amendments proposed in the present document consists in having the proposed amendments approved by the Special Committee – Regulatory Division of the Bourse. Once the approval of the Special Committee obtained, the project is simultaneously published by the Bourse for a 30-day comment period and submitted to the Autorité des marchés financiers for approval, and to the Ontario Securities Commission for information.

## **III REFERENCES**

- Rule Seven of Bourse de Montréal Inc.;
- Policy C-3 of Bourse de Montréal Inc.

**JOINT REGULATORY FINANCIAL QUESTIONNAIRE AND REPORT  
GENERAL NOTES AND DEFINITIONS**

**DEFINITIONS:**

(d) **“acceptable securities locations”** means those entities considered suitable to hold securities on behalf of a Member, for both inventory and client positions, without capital penalty, given that the locations meet the requirements outlined in the segregation bylaws, rules or regulations of the Joint Regulatory Bodies including, but not limited to, the requirement for a written custody agreement outlining the terms upon which such securities are deposited and including provisions that no use or disposition of the securities shall be made without the prior written consent of the Member and the securities can be delivered to the Member promptly on demand. The entities are as follows:

## 1. Depositories

- |                   |   |
|-------------------|---|
| (a) Canada        | The Canadian Depository for Securities Limited<br>Canadian Derivatives Clearing Corporation<br>WCE Clearing Corporation   |
| (b) United States | Depository Trust Company<br>Pacific Securities Depository Trust Company<br>Midwest Securities Trust Company<br>Stock Clearing Corporation of Philadelphia<br>Options Clearing Corporation |

## (c) Other Foreign

Foreign securities depositories or clearing agencies incorporated or organized under the laws of the foreign country and operating a central system for handling securities or equivalent book-based entries in that country and subject to enabling legislation by a central government authority in the country of operation that provides for compliance and powers of enforcement over its members. The SROs will maintain and regularly update a list of those foreign depositories or clearing agencies that comply with these criteria.

2. (a) Acceptable Institutions which in their normal course of business offer custodial security services; or  
(b) Subsidiaries of Acceptable Institutions provided that each such subsidiary, together with the Acceptable Institution, has entered into a custodial agreement with the member containing a legally enforceable indemnity by the Acceptable Institution in favour of the Member covering all losses, claims, damages, costs and liabilities in respect of securities and other property held for the Member and its clients at the subsidiary's location.
3. Acceptable Counterparties - with respect to security positions maintained as a book entry of securities issued by the Acceptable Counterparty and for which the Acceptable Counterparty is unconditionally responsible.
4. Banks and Trust Companies otherwise classified as Acceptable Counterparties - with respect to securities for which they act as transfer agent and for which custody services are not being provided (in such case, a written custody agreement is not required).
5. Mutual Funds or their Agents - with respect to security positions maintained as a book entry of securities issued by the mutual fund and for which the mutual fund is unconditionally responsible.
6. Regulated entities.
7. Foreign institutions and securities dealers that satisfy the following criteria:  
(a) the paid-up capital and surplus according to its most recent audited balance sheet is in excess of Cdn. \$150 million as evidenced by the audited financial statements of such entity;  
(b) in respect of which a foreign custodian certificate has been completed and signed in the prescribed form by the Member's board of directors or authorized committee thereof;
- provided that:  
(c) a formal application in respect of each such foreign location is made by the Member to the relevant joint regulatory authority in the form of a letter enclosing the financial statements and certificate described above; and  
(d) the Member reviews each such foreign location annually and files a foreign custodian certificate with the appropriate joint regulatory authority annually.

and such other locations which have been approved as acceptable securities locations by the Joint Regulatory Body having prime jurisdiction over the Member.