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CIRCULAR
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**MARGIN AND CAPITAL REQUIREMENTS FOR OFFSET POSITIONS IN
CANADIAN DEBT SECURITIES AND RELATED FUTURES CONTRACTS**

AMENDMENTS TO ARTICLES 7204A, 9323 AND 9423

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved amendments to articles 7204A, 9323 and 9423 of the Rules of the Bourse, which deal with market risk reduction of offset positions in debt securities of different issuers and of different maturity bands. These amendments are effective immediately.

The objective of the amendments to article 7204A is to recognize for regulatory purposes the market risk reduction of offset positions in debt securities of different issuers and different maturity bands by expanding the number of permissible offsets and by reducing the margin and capital requirements. The objective of the accompanying amendments to article 9323 and 9423 is to make the offsets available for the Government of Canada bond futures contracts positions consistent with those available for Government of Canada bonds. Appendix 1 included herewith allows to compare the new margin and capital requirements with those that existed previously.

Furthermore, in order to facilitate the introduction of new products and to broaden the application of the rules, the reference to specific futures contracts on Government of Canada bonds has been replaced by a generic term to refer to this type of futures contracts.

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.

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Vice-President, Legal Affairs and Secretary

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APPENDIX 1

**OFFSET POSITIONS INVOLVING CANADIAN DEBT SECURITIES
PREVIOUS VS NEW MARGIN AND CAPITAL REQUIREMENTS**

Offset Strategy	Previous Requirements	New Requirements
Government of Canada bonds of same maturity band OR Provincial bonds of same maturity band	<i>Maturity greater than 1 year</i> Positions may be offset on a net market value basis and margin is computed on the net long or net short position. [article 7204A 1]) <i>Maturity less than 1 year</i> Margin calculated in both positions may be netted. [article 7204A 2)]	Same
Government of Canada bonds offset with provincial bonds of same maturity band	Greater of the margin required on the long or short position.	50% of the greater of the margin required on the long or short position. [article 7204A 3) A) b)]
Government of Canada bonds offset with municipal bonds of same maturity band	Greater of the margin required on the long or short position.	Same [article 7204A 3) B) h)] except where municipal has credit rating of single A or higher, 50% of the greater of the margin required on the long or short position. [article 7204A 3) A) c)]
Provincial bonds offset with municipal bonds of same maturity band	Greater of the margin required on the long or short position.	Same [article 7204A 3) B) j)] except where municipal has credit rating of single A or higher, 50% of the greater of the margin required on the long or short position. [article 7204A 3) A) e)]
Government of Canada bonds of different maturity bands	Sum of the normal margin requirement on the long and short positions.	50% of the greater of the margin required on the long or short position. [article 7204A 3) A) a)]
Government of Canada bonds offset with provincial bonds of different maturity bands	Sum of the normal margin requirement on the long and short positions.	50% of the greater of the margin required on the long or short position. [article 7204A 3) A) b)]
Provincial bonds of different maturity bands	Sum of the normal margin requirement on the long and short positions.	50% of the greater of the margin required on the long or short position. [article 7204A 3) A) d)]
Government of Canada bonds offset with GOC bond futures contracts of same maturity band *	Positions may be offset on a net market value basis.	Same [articles 9323 a) and 9423 a)]
Government of Canada bonds offset with GOC bond futures contracts of different maturity bands	Sum of the normal margin requirement on the long and short position.	50% of the greater of the margin required on the long or short position. [articles 9323 a) and 9423 a)]

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Offset Strategy	Previous Requirements	New Requirements
Provincial bonds offset with GOC bond futures contracts of same maturity band *	Greater of the margin required on the long or short position.	50% of the greater of the margin required on the long or short position. [articles 9323 b) and 9423 b)]
Provincial bonds offset with GOC bond futures contracts of different maturity bands	Sum of the normal margin requirement on the long and short position.	50% of the greater of the margin required on the long or short position. [articles 9323 b) and 9423 b)]
Municipal bonds offset with GOC bond futures contracts of same maturity band *	Greater of the margin required on the long or short position.	Sum of the normal margin requirement on the long and short position except where Municipal has credit rating of single A or higher, 50% of the greater of the margin required on the long or short position. [articles 9323 c) and 9423 c)]
Corporate bonds offset with GOC bond futures contracts of same maturity band *	Greater of the margin required on the long or short position.	Sum of the normal margin requirement on the long and short position except where Corporate has credit rating of single A or higher, greater of the margin required on the long or short position. [articles 9323 d) and 9423 d)]
* Under the previous margin requirements, to be considered in the “same maturity band”, debt securities had to mature within 3 to 11 years.		

7204A Pairing for Margin Purposes

(09.10.91, 27.05.97, 18.02.98, 19.08.98, 17.12.02, 01.01.05, 13.09.05, 27.02.06)

1) Where an approved participant

- a) owns securities described in Group I or II of article 7204 whose maturity is over one year, and
- b) has a short position in securities
 - i) issued or guaranteed by the same issuer of the securities referred to in a) (provided that for these purposes each of the provinces of Canada must be regarded as the same issuer as any other province);
 - ii) maturing over one year;
 - iii) maturing within the same periods for the purpose of determining margin rates for the securities referred to in a); and
 - iv) with a market value equal to the securities referred to in paragraph a) (with the intent that no pairing is permitted in respect of the market value of a long [or short] position which is in excess of the market value of the short [or long] position);

the two positions may be offset and the required margin must be computed with respect to the net long or net short position only. This rule also applies to future purchase and sale commitments.

2) Where an approved participant

- a) owns securities described in Group I or II of article 7204 maturing within one year, and
- b) has a short position in securities
 - i) issued or guaranteed by the same issuer of the securities referred to in a) (provided that for these purposes, each of the provinces of Canada must be regarded as the same issuer as any other province);
 - ii) maturing within one year; and
 - iii) with a market value equal to the securities referred to in paragraph a) (with the intent that no offset is permitted in respect of the market value of a long [or short] position which is in excess of the market value of the short [or long] position);

then the margin required must be the excess of the margin on the long (or short) position over the margin required on the short (or long) position. This rule also applies to future purchase and sale commitments.

3) A) Where an approved participant has a short and long position in the following groups of securities of article 7204, the total margin required in respect of both positions must be 50% of the greater of the margin required on the long or short position:

Long (Short)		Short (Long)
a) Group I (Canada only)	and	Group I (Canada only with different maturity bands)
b) Group I (Canada only)	and	Group II (province of Canada only with identical or different maturity bands)
c) Group I (Canada only)	and	Group III (municipality of Canada only)
d) Group II (province of Canada only)	and	Group II (province of Canada only with different maturity bands)
e) Group II (province of Canada only)	and	Group III (municipality of Canada only)

- B) Where an approved participant has a short and long position in the following groups of securities of article 7204, the total margin required in respect of both positions must be the greater of the margin required on the long or short position:

Long (Short)		Short (Long)
f) Group I (U.S. Treasury only)	and	Group I (Canada only)
g) Group I (U.S. Treasury only)	and	Group II (province of Canada only)
h) Group I (Canada and	and	Group III (municipality of Canada only) U.S. Treasury only)
i) Group I (Canada and U.S. Treasury only)	and	Group V (corporate)
j) Group II (province of Canada only)	and	Group III (municipality of Canada only)
k) Group II (province of Canada only)	and	Group V (corporate)
l) Group V (corporate)	and	Group V (corporate of the same issuer)

- C) Furthermore, the offsets described above in paragraphs A) and B) may only apply if the following requirements are complied with:

- i) securities offsets described in subparagraphs a), b) and d) can be of different maturity bands, all other offsetting positions must mature within the same periods referred to in article 7204 for the purpose of determining margin rates;
- ii) securities described in Group III (municipality of Canada) of article 7204 are eligible for offsets described in subparagraphs c) and e) only if they have a long-term issuer credit rating of a single A or higher by any of Canadian Bond Rating Service, Dominion Bond Rating Service, Moody's Investors Service or Standard & Poor's Bond Record;

- iii) securities described in Group V (corporate) of article 7204 and securities described in article 7205 are eligible for offset only if they are not convertible and have a single A or higher rating by any of Canadian Bond Rating Service, Dominion Bond Rating Service, Moody's Investors Service or Standard & Poor's Bond Record;
- iv) securities in offsetting positions must be denominated in the same currency; and
- v) the market value of the offsetting positions is equal and no offset is permitted in respect of the market value of the short (or long) position which is in excess of the market value of the long (or short) position.

For the purpose of this article, securities described in article 7205 are eligible for an offset identical to the one applicable to securities described in Group V of article 7204.

9323 Futures Contracts and Security Combinations

(01.01.05, 27.02.06)

With respect to futures contracts and securities (including future purchase and sale commitments) held in a client's account, the combinations described in paragraphs a) to e) may only apply if the following requirements are complied with:

- i) securities described in Group III (municipality of Canada) of article 7204 are eligible for offset only if they have a long-term issuer credit rating of a single A or higher by any of Canadian Bond Rating Service, Dominion Bond Rating Service, Moody's Investors Service or Standard & Poor's Bond Record;
- ii) securities described in Group V (corporate) of article 7204 are eligible for offset only if they are not convertible and have a single A or higher rating by any of Canadian Bond Rating Service, Dominion Bond Rating Service, Moody's Investors Service or Standard & Poor's Bond Record;
- iii) securities in offsetting positions must be denominated in the same currency; and
- iv) the market value of the offsetting positions is equal and no offset is permitted in respect of the market value of the short (or long) position which is in excess of the market value of the long (or short) position.

For the purpose of this article, maturity bands are the one referred to in article 7204 for the purpose of determining margin rates.

a) Bond futures contracts combinations with Group I securities

Where a client account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in Government of Canada securities as described in Group I of article 7204, and the offsetting positions are maturing within the same maturity band, the total margin required in respect of both positions must be the margin required on the net long or short position;

Where a client account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in Government of Canada securities as described in Group I of article 7204, and the offsetting positions are of different maturity bands, the total margin required in respect of both positions must be 50% of the greater of the margin required on the long or short position.

b) Bond futures contracts combinations with Group II securities

Where a client account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in Province of Canada securities as described in Group II of article 7204, and the offsetting positions are maturing within the same or different maturity bands, the total margin required in respect of both positions must be 50% of the greater of the margin required on the long or short position.

c) Bond futures contracts combinations with Group III securities

Where a client account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in municipality of Canada securities as described in Group III of article 7204, and the offsetting positions are maturing within the same maturity band, the total margin

required in respect of both positions must be 50% of the greater of the margin required on the long or short position.

d) Bond futures contracts combinations with Group V securities

Where a client account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in corporation securities as described in Group V of article 7204, and the offsetting positions are maturing within the same maturity band, the total margin required in respect of both positions must be the greater of the margin required on the long or short position.

e) Canadian bankers' acceptance futures contracts combinations with bankers' acceptance

Where a client account contains a long (short) 3-month Canadian bankers' acceptance (BAX) futures contracts position and a short (long) position in a bankers' acceptance issued by a Canadian chartered bank, the total margin required in respect of both positions must be the greater of the margin required on the long or short position.

9423 Futures Contracts and Security Combinations

(00.00.04, 27.02.06)

With respect to futures contracts and securities (including future purchase and sale commitments) held in an approved participant's account, the combinations described in paragraphs a) to e) may only apply if the following requirements are complied with:

- i) securities described in Group III (municipality of Canada) of article 7204 are eligible for offset only if they have a long-term issuer credit rating of a single A or higher by any of Canadian Bond Rating Service, Dominion Bond Rating Service, Moody's Investors Service or Standard & Poor's Bond Record;
- ii) securities described in Group V (corporate) of article 7204 are eligible for offset only if they are not convertible and have a single A or higher rating by any of Canadian Bond Rating Service, Dominion Bond Rating Service, Moody's Investors Service or Standard & Poor's Bond Record;
- iii) securities in offsetting positions must be denominated in the same currency; and
- iv) the market value of the offsetting positions is equal and no offset is permitted in respect of the market value of the short (or long) position which is in excess of the market value of the long (or short) position.

For the purpose of this article, maturity bands are the one referred to in article 7204 for the purpose of determining margin rates.

a) Bond futures contracts combinations with Group I securities

Where an approved participant account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in Government of Canada securities as described in Group I of article 7204, and the offsetting positions are maturing within the same maturity band, the total capital required in respect of both positions must be the capital required on the net long or short position;

Where an approved participant account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in Government of Canada securities as described in Group I of article 7204, and the offsetting positions are of different maturity bands, the total capital required in respect of both positions must be 50% of the greater of the capital required on the long or short position.

b) Bond futures contracts combinations with Group II securities

Where an approved participant account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in Province of Canada securities as described in Group II of article 7204, and the offsetting positions are maturing within the same or different maturity bands, the total capital required in respect of both positions must be 50% of the greater of the capital required on the long or short position.

c) Bond futures contracts combinations with Group III securities

Where an approved participant account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in municipality of Canada securities as described in Group III of article 7204, and the offsetting positions are maturing within the same maturity band, the total capital required in respect of both positions must be 50% of the greater of the capital required on the long or short position.

d) Bond futures contracts combinations with Group V securities

Where a client account contains a long (short) Government of Canada bond futures contracts position and a short (long) position in corporation securities as described in Group V of article 7204, and the offsetting positions are maturing within the same maturity band, the total capital required in respect of both positions must be the greater of the capital required on the long or short position.

e) Canadian bankers' acceptance futures contracts combinations with bankers' acceptance

Where an approved participant account contains a long (short) 3-month Canadian bankers' acceptance (BAX) futures contracts position and a short (long) position in a bankers' acceptance issued by a Canadian chartered bank, the total capital required in respect of both positions must be the greater of the capital required on the long or short position.