☒	**Trading – Interest Rate Derivatives**	☒	**Back-office - Options**
☒	**Trading – Equity and Index Derivatives**	☒	**Technology**
☒	**Back-office – Futures**	☒	**Regulation**

CIRCULAR
March 31, 2008

EXCHANGE FOR PHYSICAL AND EXCHANGE OF OVER-THE-COUNTER DERIVATIVE INSTRUMENTS

ABROGATION OF ARTICLE 6006 AND AMENDMENTS TO ARTICLES 6005 AND 6815

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved the abrogation of article 6006 of the Rules of the Bourse and amendments to articles 6005 and 6815 of these Rules. The amended articles are in respect of over-the-counter transactions and more particularly in respect of exchange for physical and exchange of over-the-counter derivative instruments. All these changes to the Rules of the Bourse will become effective on April 21, 2008.

Nature of amendments to the Rules of the Bourse

Article 6005 – Off-Exchange Transactions

This article of the Rules of the Bourse which lists what are the off-exchange transactions permitted by the Bourse included many provisions that had become obsolete following the specialization of the Bourse in the derivative instruments market. All obsolete provisions have therefore been deleted and article 6005 will now contain only the off-exchange transactions that are still relevant for the Bourse.

Article 6006 – Trades outside Canada

This article, which was permitting at certain conditions the execution of off-exchange transactions with persons not residing in Canada, has been entirely abrogated since it was applicable only to the equity market, a market on which the Bourse is no longer carrying on any activities since it started its specialization in derivative instruments.

Article 6815 – Exchanges for Physicals (EFP)

Article 6815 of the Rules of the Bourse which previously covered only Exchanges for Physical transactions (EFP) has been subjected to a major revision. Not only has its wording itself been revised to facilitate the interpretation and the application of the Rule, but new important elements have been introduced to allow broadening the scope of possible transactions in futures contracts. Important restrictions have also been eliminated in order to facilitate the use of the transactions that fall under the scope of this article.

Circular no.: 049-2008
Amendment no.: 004-2008

The most important addition to this article and to the services offered by the Bourse, is that market participants will now have the possibility to execute not only transactions that involve the exchange of a cash instrument against futures contracts listed on the Bourse (EFP), but also transactions involving the exchange of over-the-counter derivative instruments against futures contracts ("Exchange for Risk Transactions" or EFR). The addition of this new type of transactions will allow providing market participants with an additional tool for managing their portfolio risks. The Bourse took care to ensure that the number of over-the-counter derivative instruments eligible to that type of transactions be as large as possible in order to encourage the use of such transactions. You will find in the Appendix of the Procedure applicable to EFP and EFR transactions a complete list of these eligible over-the-counter derivative instruments.

Also, former article 6815 included a very important restriction in respect of the price at which the future contract leg of an EFP transaction could be executed. It was effectively provided that the price of the future contract leg of any EFP transaction executed between two approved participants had to be between the high and low prices of the trading session during which the EFP transaction was executed. Such a restriction is no longer justified in reason of the fact that the Bourse and the clearing corporation now have technological tools allowing to manage risks on a practically real time basis. This price restriction has therefore been eliminated and replaced by the "fair and reasonable" price concept that has now been applied by the Bourse for a few years in respect of block transactions. The elimination of this restriction should allow market participants to have an increased flexibility when preparing an EFP transaction. It is to be noted that the fait and reasonable price concept applies to EFP transactions as well as EFR transactions.

For what regards price restrictions that existed on the cash leg of an EFP transaction, they have been entirely abrogated.

The Bourse also added to article 6815 provisions respecting the beneficial ownership of accounts that are involved in an EFP or EFR transactions. The general principle is that these accounts must have different beneficial owners. However, the execution of transactions between accounts that have the same beneficial owner may be permitted subject to certain conditions specified in paragraph h) of article 6815 and provided that it can be demonstrated that the transaction was executed at the same conditions as an arm's length transaction.

Finally, another new provision has been added to article 6815 in order to specify that it is prohibited to execute an EFP or EFR transaction for the sole purpose of circumventing the contract month roll.

<u>Procedure for the execution and reporting of Exchange for Physical (EFP) and Exchange for Risk (EFR) transactions</u>

In connection with amendments made to article 6815 of its Rules, the Bourse also updated it written procedures that are applicable to the execution of EFP transactions by incorporating therein EFR transactions. In general, EFR transactions are subjected to the same regulatory requirements as those that are applicable to EFP transactions. This should facilitate the execution of these two types of transactions. As already mentioned, a list of over-the-counter derivative instruments that are acceptable for the purpose of EFR operations has been added as an Appendix to the procedures. Procedures of the Bourse can be accessed at any time on the Website of the Bourse in the official practices section (http://www.m-x.ca/publi_pratiq_officiel_en.php).

Finally, the report form that must be used for the EFR transactions is the same as the one prescribed for EFP transactions. This form is available on the Website of the Bourse at http://www.m-x.ca/efp_formulaire_en.php .

Comments received

The regulatory amendments that are discussed in this circular were subjected to a request for comments published by the Bourse. In the case of the rules respecting EFR transactions, the Bourse published its request for comments on September 28, 2006 (Circular No. 162-2006) while in the case of the rules respecting EFR transactions, the request for comments was published on February 15, 2007 (Circular No. 028-2007)

Following the publication of these requests for comments, the Bourse received two comment letters. As required by the Autorité des marches financiers, the Bourse must publish, when implementing a regulatory amendment, a summary of comments received following the request for comments as well as the response of the Bourse to these comments. You will therefore find as an Appendix to this circular the said summary as well as the Bourse's responses to the comments received.

For further information, please contact Richard Bourbonnière, Vice-President, Market Operations, Financial Markets, at 514 871-3548 or at rbourbonniere@m-x.ca.

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

6005 Off-Exchange Transactions
(10.10.91, 19.11.93, 14.07.95, 22.11.99, 21.04.08)

The only transactions in any securities or derivative instruments listed on the Bourse which an approved participant may make off the Bourse are the following:

a) a transaction made to adjust an execution error on a client's order;

b) a transaction made as a result of the exercise of an option or of a delivery pursuant to a futures contract;

c) an Exchange for Physicals (EFP) transaction or an Exchange for Risk (EFR) transaction pursuant to article 6815;

d) an off-exchange transfer of securities or derivative instruments pursuant to article 6816;

e) a block trade in a security or derivative instrument designated by the Bourse and executed according to the provisions of article 6380.

6006 Trades Outside Canada
(10.10.91, abr. 21.04.08)

6815 Exchanges for Physicals (EFP) and Exchanges for Risk Transactions (EFR)
(08.09.89, 17.10.91, 05.01.94, 19.01.95, 01.05.95, 07.09.99, 31.01.01, 03.05.04, 21.04.08)

Exchanges for physicals (EFP) or exchanges for risk (EFR) transactions involving futures contracts listed and traded on the Bourse are permitted if such transactions are executed in accordance with the requirements of this article and of the procedures established by the Bourse.

1) Exchanges for physicals (EFP)

a) An EFP may be concluded between two parties if one of the parties is the buyer of a physical or cash component that is acceptable to the Bourse for the purpose of the EFP transaction and the seller of the futures contract, and the other party is the seller of such physical or cash component and the buyer of the futures contract.

b) The purchase and sale of the futures contract must be simultaneous with the sale and purchase of a corresponding quantity of the physical or cash component acceptable to the Bourse for the purpose of the EFP transaction.

2) Exchange for Risk Transactions

An exchange of a futures contract for an over-the-counter (OTC) derivative instrument and/or swap agreement (an Exchange for Risk (EFR) transaction) consists of two discrete, but related simultaneous transactions: a risk transaction and a futures contract transaction. At the time such transaction is effected, the parties to the futures contract transaction must be the same parties to the risk transaction and the buyer and the seller of the futures contract must be, respectively, the seller and the buyer of the OTC derivative instrument and/or swap agreement. The risk component of the EFR transaction must involve an OTC derivative instrument and/or swap agreement that is related to and that has a reasonable price correlation with the underlying interest of the futures contract being exchanged. The quantity or value covered by the risk component of the EFR transaction must be approximately equivalent to the quantity or value covered by the futures contract.

3) General Provision

a) EFP and EFR transactions must at all times be executed in accordance with such other procedures, terms and conditions that the Bourse may prescribe from time to time.

b) The futures contracts that are eligible to EFP or EFR transactions, and the last day and time for executing such transactions shall be determined by the Bourse.

c) The cash components acceptable for the purpose of an EFP transaction and the over the counter derivative instruments acceptable for the purpose of an EFR transaction are those specified in the procedures set by the Bourse.

d) Each party to an EFP or EFR transaction must satisfy the Bourse, upon request, that the transaction is a bona fide EFP or EFR transaction. To this effect, parties to such a transaction must maintain and must provide to the Bourse upon request complete records and documentary evidence relating to such transaction including all records relating to the purchase or sale of securities, physical underlyings, sub-instruments of these physical underlyings, instruments related thereto or over the counter derivative instruments and to any transfer of funds or ownership made in connection with such transaction.

e) It is prohibited for any party to an EFP or an EFR transaction to effect a transaction which is contrary to the requirements and practices prescribed by the rules, policies and procedures of the Bourse or to effect such a transaction for the sole purpose of reporting, registering or recording a price that is not a bona fide price or of making a transaction which is a "wash sale", an accommodation trade or a fictitious sale.

f) An EFP or an EFR transaction may be made at such prices that are mutually agreed upon by the two parties to this transaction. However, the price at which the futures contract leg of the transaction is arranged must be fair and reasonable in light of factors such as, but not limited to, the size of the transaction, the currently traded prices and bid and ask prices in the same contract at the relevant time, the volatility and liquidity of the relevant market as well as the general market conditions.

g) Each EFP or EFR transaction must be reported to the Bourse in accordance with the procedures set by the Bourse. Such report must be in the form prescribed by the Bourse and must contain all the information required on such prescribed form.

h) Each EFP or EFR transaction executed during the usual trading hours of the futures contract to which the transaction applies must be immediately reported to the Bourse. Each EFP or EFR transaction executed after the usual trading hours of the futures contract to which the transaction applies must be reported to the Bourse no later than 10:00 a.m. (Montréal time) on the next trading day following the execution of the transaction.

i) The accounts involved on each side of an EFP or EFR transaction must satisfy at least one of the following conditions:

   i) they have different beneficial ownership;

   ii) they have the same beneficial ownership, but are under separate control;

iii) the accounts are commonly controlled, but involve separate legal entities which may or may not have the same beneficial ownership.

In cases where the parties to an EFP or EFR transaction involve the same legal entity, same beneficial ownership, or separate legal entities under common control, the parties must be able to demonstrate that the exchange transaction was a legitimate arms-length transaction.

j) It is strictly prohibited for any party, for both the buyer and the seller, to enter into an EFP or EFR transaction to circumvent the contract month roll in the corresponding security or derivative instrument.

PROCEDURE FOR THE EXECUTION AND REPORTING OF EXCHANGE FOR PHYSICAL (EFP) AND EXCHANGE FOR RISK (EFR) TRANSACTIONS

The purpose of the following procedure is to explain as fully as possible the requirements of article 6815 of the Rules of Bourse de Montréal Inc. (the Bourse) relating to the execution of transactions involving the exchange of futures contracts for a corresponding cash position (Exchange for Physical (EFP) and of transactions involving the exchange of futures contracts for a corresponding over-the-counter derivative instrument (Exchange for Risk (EFR)). Approved participants must ensure that all of their employees who are involved in the execution of this type of transactions are fully aware of this procedure. Any violation of the requirements set forth in article 6815 of the Rules of the Bourse and in this procedure could result in disciplinary action being taken by the Bourse.

Exchanges for Physicals (EFP)

An EFP is a transaction whereby two parties enter into an agreement in which one party purchases a cash market position and simultaneously sells a corresponding futures contract position and the other party sells the cash market position and simultaneously purchases the corresponding futures contract position.

The Bourse currently permits EFP transactions on the following futures contracts: Thirty-Year Government of Canada Bond futures contract (LGB), Ten-Year Government of Canada Bond futures contract (CGB), Two-Year Government of Canada Bond futures contract (CGZ), S&P Canada 60 Index futures contract (SXF) and sectorial index futures contracts (SXA, SXB, SXH and SXY).

Exchange for Risk (EFR)

An EFR is a transaction whereby two parties enter into an agreement in which one party purchases an over-the-counter derivative instrument and simultaneously sells a corresponding futures contract and the other party sells the over-the-counter derivative instrument and simultaneously purchases the corresponding futures contract.

The Bourse currently permits EFR transactions on the following futures contracts: Government of Canada Bond futures contracts (LGB, CGB and CGZ), short-term interest rate futures contracts (BAX and ONX), and stock index futures contracts (SXF, SXA, SXB, SXH and SXY).

Pricing the Cash component of an EFP or the Risk component of an EFR

The cash component of an EFP or the risk component of an EFR is priced at such level that is mutually agreed upon by the two parties to the transaction.

The futures contract leg of an EFP or an EFR must be priced at a fair and reasonable level in light of factors such as, but not limited to, the size of such an EFP or EFR transaction, the currently traded prices and bid and ask prices in the same contract at the relevant time, the volatility and liquidity of the relevant market and the general market conditions prevailing at the time the EFP or EFR transaction is executed.

The cash component of an EFP or the risk component of an EFR transaction must be the futures contract underlying interest, a by-product of this underlying interest or a similar product that is reasonably correlated to the futures contract being exchanged. Approved participants who are parties to an EFP or an EFR transaction may be required to demonstrate that the cash market component of such an EFP or the risk component of such an EFR and the futures contract position are sufficiently correlated to make the transaction acceptable to the Bourse.

Also, the number of futures contracts exchanged must be approximately equivalent to the quantity or value of the cash market position being exchanged in an EFP transaction or of the risk component being exchanged in the case of an EFR. Approved participants that are parties to an EFPor an EFR transaction may be required to demonstrate such equivalency.

Acceptable EFP and EFR Transactions

In order to have an EFP or an EFR transaction accepted by the Bourse, the transaction must satisfy the following conditions:

- There must be separate but integrally related futures contracts and cash (in the case of an EFP) or risk component (in the case of an EFR) transactions.

- The exchange transaction must be done between two separate accounts that must satisfy at least one of the following criteria:
  - accounts have different beneficial ownership;
  - accounts have the same beneficial ownership but are under separate control; or
  - accounts are under a common control but involve separate legal entities which may or may not have the same beneficial ownership.

  If the parties to an EFP or EFR transaction involve the same legal entity, same beneficial owner or separate legal entities under common control, the approved participant (or the parties themselves) must be able to demonstrate that the EFP or EFR transaction is a legitimate arm's length transaction.

- The cash market instrument leg of the EFP or the risk component leg of an EFR transaction must provide for a transfer of ownership of the cash market instrument of an EFP or of the over-the-counter derivative instrument of the EFR to the buyer of this instrument and the delivery of this instrument must take place within a reasonable period of time (in accordance with cash market or over-the-counter practice).

- The relation between the prices of the futures contract and of the cash instrument leg of the EFP or the risk component leg of the EFR transaction and the relevant prices in either market must be established.

- If he does not have actual possession of the cash instrument, in the case of an EFP transaction, or of the over-the-counter derivative instrument, in the case of an EFR transaction, before the execution of the transaction, the seller of this cash instrument or over-the-counter derivative instrument must be able to demonstrate his ability to satisfy his delivery obligation.

Acceptable Cash Components for the purpose of an EFP Transaction

In order to have an EFP transaction accepted by the Bourse, the cash component of the transaction must satisfy the following conditions:

- **For interest rate futures contracts (LGB, CGB and CGZ):** all maturities of Government of Canada fixed income bonds that are reasonably correlated to the futures contract being exchanged. Approved participants involved in an EFP transaction may be required to demonstrate that the related cash bond position and the futures contract position are reasonably correlated.

- **For stock index futures contracts (SXF and sectorial indexes):** stock baskets must be reasonably correlated to the underlying index with a correlation coefficient (R^2) of 0.90 or more. Furthermore, these stock baskets must represent a weight of at least 50% of the underlying index or must include at least 50% of the securities of the underlying index. The notional value of the basket must be fairly equal to the value of the futures contract component of the exchange transaction. Exchange Traded Funds (iShares™) are also acceptable, provided they mirror the index futures contract against which the EFP transaction is made.

Permissible Over-the-Counter Derivative Instruments for the purpose of an EFR Transaction

A list of permissible over-the-counter derivative instruments for the purpose of effecting an EFR transaction is included in Appendix I.

As a guideline, the time period used to calculate the correlation coefficient must be based on daily price data for a period of at least six (6) months or, if weekly price data are used, for a period of at least one (1) year

Reporting an EFP or EFR transaction to the Bourse

EFP and EFR transactions must be reported to the Bourse's Market Monitoring Department for approval and subsequent input into the Montréal Automated System (SAM). Approved participants for both the seller and buyer must complete and submit to the Market Monitoring Department the EFP / EFR reporting form prescribed by the Bourse. This form is available on the website of the Bourse at http://www.m-x.ca/efp_formulaire_en.php. If the EFP or EFR transaction is executed before the closing of the trading session of the futures contract involved in the transaction, the EFP / EFR reporting form must be submitted immediately upon the execution of the transaction. If the EFP or EFR transaction is made after the closing of the trading session, the EFP / EFR reporting form must be submitted no later than 10:00 a.m. (Montréal time) on the next trading day.

If the EFP / EFR reporting form is not accurately filled out with all the relevant information required by the Market Monitoring Department of the Bourse, the transaction will not be approved neither recorded in SAM and the approved participant will have to resubmit a new EFP / EFR reporting form correctly completed.

Once correctly completed EFP / EFR reporting forms have been received, the Market Monitoring Department will validate the transaction. The Bourse has the discretion to refuse an EFP or EFR transaction if it deems that it is not in compliance with the requirements of article 6815 of the Rules of the Bourse or of this procedure. In case of refusal, the Market Monitoring Department will ensure that the approved participant(s) involved in the EFP or EFR transaction are promptly informed of such refusal and of the reasons for it.

Once an EFP or an EFR transaction has been validated and has been entered into SAM by the Market Monitoring Department, the following information with respect to this transaction will be disseminated by the Bourse on its website at http://www.m-x.ca/dailycrosses_en.php.

- Date and time of transaction
- product description (code);
- Contract month(s);
- Volume of the transaction; and
- Transaction price

Trade validation and market dissemination by the Bourse of an EFP or EFR transaction will not preclude the Bourse from initiating any investigation and, as the case may be, disciplinary procedures in the event that the transaction is subsequently found to have been made other than in accordance with the requirements of article 6815 of the Rules of the Bourse or of this procedure.

Audit Trail Requirements for EFP and EFR Transactions

Approved participants who enter into an EFP or EFR transaction must maintain all documents relevant to the futures contracts and corresponding cash market or over-the-counter derivative instruments transactions and must be able to promptly provide copies of such documents to the Regulatory Division of the Bourse upon request. Documents that may be requested include, but are not limited to, the following:

- Futures contracts order tickets;
- Futures contracts account statements;
- Documentation customarily generated in accordance with the cash market, over-the-counter or other relevant market practices such as cash account statements, trade confirmation statements, ISDA® Master Agreements or other documents of title;
- Third party documentation to support proof of payment or allowing to verify that the ownership title of the related cash market position or, as the case may be, of the related over-the-counter derivative instrument position was transferred from the seller to the buyer. This may include, but is not limited to canceled checks, bank statements; cash account statements and cash instruments clearing corporation documents (e.g.: CDS Depository and Clearing Services Inc.).

All futures contracts order tickets must clearly indicate the time of execution of the EFP or EFR transactions.

Exchange for Risk: List of permissible OTC derivative instruments

	Bond Futures Contracts	Short-Term Interest Rate Futures Contracts	Stock Index Futures/ Single Stock Futures	Commodities Futures
Vanilla Interest Rate Swaps	√	√		
Equity and Index Swaps			√	
Commodities Swaps or Forwards				√
Forward Rate Agreements - FRAs		√		
OTC Options and Options Strategies	√	√	√	

The following outlines the characteristics of OTC derivative instruments that would be acceptable for EFR transaction purposes.

Swaps:

Interest rate

- standard plain vanilla OTC swap;
- written under the terms of an ISDA® Master Agreement;
- providing for regular fixed rate payments against regular floating rate payments;
- All swap payments must be denominated in the currency of a G7 member country;
- The OTC interest rate swap must be reasonably correlated with an $R^2 = 0.90$ or greater so that the futures contract is a suitable instrument for hedging the OTC derivative instrument transactions. As a guideline, the time period used to calculate the correlation must be based on daily price data for a period of at least six (6) months or, if weekly price data are used, for a period of at least one (1) year.

Equities and Indices

- standard plain vanilla OTC swap;
- written under the terms of an ISDA® Master Agreement;
- providing for regular fixed rate payments or regular floating rate payments against the positive or negative performance of a basket of securities or a stock index;
- All swap payments must be denominated in the currency of a G7 member country;

- The OTC equity or index swap must be reasonably correlated with an $R^2 = 0.90$ or greater so that the futures contract is a suitable instrument for hedging the OTC derivative instrument transaction. As a guideline, the time period used to calculate the correlation must be based on daily price data for a period of at least six (6) months or, if weekly price data are used, for a period of at least one (1) year.

Swaps or forwards on Commodities :

- written under the terms of an ISDA® Master Agreement;
- The OTC commodities swap or forward must be reasonably correlated with an $R^2 = 0.80$ or greater so that the futures contract is a suitable instrument for hedging the OTC derivative instrument transaction. As a guideline, the time period used to calculate the correlation must be based on daily price data for a period of at least six (6) months or, if weekly price data are used, for a period of at least one (1) year.

Forward Rate Agreements (FRAs):

- conventional FRA;
- written under the terms of an ISDA® Master Agreement;
- predetermined interest rate;
- agreed start/end date;
- have a defined interest (repo) rate.

OTC Options and OTC Option strategies:

- Any individual or combination of OTC equity or stock index option positions can form the risk transaction component of an EFR transaction against any of the Bourse's stock index or single stock futures contracts.
- Any individual or combination of OTC bond, interest rate swap or FRA options (e.g. caps, floors, collars) can form the risk component of an EFR transaction against any of the Bourse's interest rate futures contracts

Bonds used in an EFR transaction must have the following characteristics:

- fixed coupon rate;
- bullet maturity issue (a coupon paying bond with no repayment of principal until maturity);
- no embedded optionality or early redemption features;
- an ISIN code;
- fixed principal amount;

- denominated in the currency of a G7 member country.

Stock Baskets used in an EFR transaction must have the following characteristics:

- be reasonably correlated to the index underlying the futures contract with an R^2 = 0.90 or greater and the time period used to calculate the correlation must be based on daily price data for a period of at least six (6) months or, if weekly price data is used, for a period of at least one (1) year;

- represent at least 50% of the weight of the index underlying the futures contract or include at least 50% of the stocks comprised in the index underlying the futures contract;

- have a notional value equivalent to the value of the futures contract component of the EFR transaction;

- exchange traded funds (ETFs) are acceptable provided that they mirror stock index products traded on the Bourse.

Exchange for Physical (EFP) and Exchange for Risk (EFR)
Reporting Form
General Information

Individual submitting report

Name:*

Title:*

Approved participant:*

SAM authorized person executing EFP / EFR transaction

Name:*

SAM user id:*

Phone:*

Fax:

Details of the EFP / EFR

Counterparty name:*

Trade date and time:* DD

hh : 00 a.m.

Futures contract component

Symbol:*

Quantity:*

Contract month & year:* MM - YY

Buyer:*

Seller:*

EFP / EFR Price:*

Cash Component of EFP / Risk Component of EFR

Description:*

Quantity or Value*

Buyer:*

Seller:*

Applicable market value per unit:*

Additional Details :

Envoyer

The transmission of the above information to the Bourse and the subsequent validation and dissemination of the transaction by the Market Monitoring Department will not preclude the Bourse from initiating any analysis and/or investigation to ensure that the transaction has been made in accordance with the requirements of the Rules of the Bourse or of the Procedure for the Execution of EFP and EFR Transactions. If, following such analysis or investigation, it appears that the transaction was not in full compliance with applicable regulatory requirements, the Bourse has the discretion to initiate a disciplinary process.

COMMENTS ON PROPOSED AMENDMENTS TO ARTICLE 6815 – EXCHANGES FOR PHYSICALS AND EXCHANGES FOR RISK TRANSACTIONS.

Comments Author	Comments	Reply to Comments
J.P. Morgan Securities Canada Inc.	J.P. Morgan Securities Canada Inc. (JPMSCI) is supportive of the proposed amendments to articles 6005 and to article 6815. JPMSCI asks that the implementation of the amendments be as non-restrictive as possible. In that respect it is suggested that there be no minimum size requirements placed on EFRs and that what constitutes the "risk" component be liberally construed while maintaining an appropriate relationship to the futures component of such a transaction.	There is no minimum size requirement threshold to execute an EFR. This is consistent with the approach that there is no minimum size requirement to execute an EFP. However, the Bourse must retain the requirement that the quantity covered by the risk component of the EFR must be equivalent to the value covered by the futures contract (as specified in the last sentence of paragraph 2 of article 6815). As is the case for the cash leg of an EFP, the dollar value of the risk leg of an EFR must be equivalent to the dollar value of the futures contracts leg. For example, in an EFP on a 10-year CGB bond futures contract, the dollar value of the cash bonds exchanged for the CGB contract must be equivalent to the dollar value of the future contract. Excluding transaction costs or other operational costs between participants, there cannot be a disconnect between the two amounts. Furthermore, the terminology adopted by the Bourse is consistent with the terminology adopted by other exchanges such as the CME and NYMEX and by the CFTC in its guidelines. In reference to the comment on the "risk component", this component can be liberally interpreted provided that: 1. the OTC derivative instrument representing the risk component of an EFR transaction must have the characteristics set forth in the "List of permissible OTC derivative instruments", and, 2. there is an appropriate correlation between the risk component of the EFR and the futures contract as defined in the "List of permissible OTC derivative instruments". Additional OTC derivative instruments may eventually be added to the "List of permissible OTC derivative instruments" if market participants express their interest to have such instruments included and that such inclusion is justified.

COMMENTS ON PROPOSED AMENDMENTS TO ARTICLE 6815 – EXCHANGES FOR PHYSICALS AND EXCHANGES FOR RISK TRANSACTIONS.

Comments Author	Comments	Reply to Comments
Merrill Lynch Canada Inc.	Merrill Lynch agrees with the rationale of the proposal on Exchange for Physical transactions (EFP) and believes it is not practical to restrict the pricing of the futures leg contract of an EFP between the high and low of the trading day. They do request further clarification on the term "fair and reasonable".	The Bourse is adopting the term "fair and reasonable" consistent with the same terminology used for Block Trades under article 6380 of the Rules of the Bourse and to be consistent with the terminology adopted by U.S. exchanges. The Bourse will consider an EFP trade price to be "fair and reasonable" as the price that an approved participant considers the best available price for a transaction of similar type and size. In considering whether or not an EFP transaction price is fair and reasonable the Bourse will take into account: (i) the size of the EFP; and (ii) the price and size of other trades in any relevant markets at the applicable time and the circumstances of the market or the parties to the EFP trade. Relevant markets could include, without limitation, the contract market itself, the underlying cash markets and/or other related futures markets. A participant effecting an EFP trade could execute an EFP transaction at a price that was away from the market provided that the participant retains documentation to demonstrate that the price was indeed fair and reasonable under the participant's or market's particular circumstances. Therefore, an EFP trade price negotiated outside the current bid/ask price and outside the high/low price of the day should consider: 1. how the EFP trade price reflects commercial realities; or 2. the particular "circumstances" of the participants or of the markets. An example of a "fair and reasonable" price for the futures contract leg of an EFP that is reported outside the current bid/ask and high/low price occurs in a situation where a market participant reports the EFP price at a volume weighted average price (VWAP) based on multiple cash market transactions. The VWAP method is often used by market participants to split a large trade into multiple transactions when such a transaction cannot be executed in its entirety at one price without impacting the market. The VWAP is represented as the sum of the value (price * volume) of each trade during the period divided by the total volume for the period.

COMMENTS ON PROPOSED AMENDMENTS TO ARTICLE 6815 – EXCHANGES FOR PHYSICALS AND EXCHANGES FOR RISK TRANSACTIONS.

Comments Author	Comments	Reply to Comments
	Merrill Lynch supports the use of the new standardized reporting form that has been implemented by the Bourse. They suggest this standardized form include a section to detail the breakdown of contracts and different prices for a basket of securities for an index futures contract.	A section entitled “Additional Details” is already included at the bottom of the reporting form where approved participants can enter the breakdown of contracts and the different prices of the cash leg of the EFP transaction. Approved participants may also use this section to specify any other details that may be pertinent to the transaction reported to the Bourse. (refer to the Web site of the Bourse at http://www.m-x.ca/efp_formulaire_en.php for the Reporting Form)
	Merrill Lynch believes that incorporating a new provision in article 6815 prohibiting EFP transactions for the sole purpose of circumventing the contract month roll in the corresponding security or derivative instrument (paragraph j)could potentially harm the ability of participants to service their clients. Merrill Lynch is often requested to call a basis market on multiple contract months. They would like to better understand why other major derivatives exchanges have chosen to include this prohibition. They also request further clarification on the term sole purpose in paragraph j) of article 6815, as this concept could potentially be open to interpretation by different parties.	The intent of the roll prohibition is not to prohibit EFPs during the roll period, but to prohibit EFPs executed in order to circumvent the roll with the purpose of by-passing the central order book to offset pre-existing futures positions. The rationale behind this prohibition used by the Sydney Futures Exchange (SFE) and the Chicago Board of Trade (CBOT) is to get as much volume activity as possible going through the central order book when liquidity is usually at its peak during the roll period. For example, the Bourse would not permit EFPs by a participant if on a trading day during the roll period this participant systematically executes multiple EFPs for the purpose of offsetting that participant’s entire open position and with the intent of by-passing the contract month roll. Such action by the participant would be deemed to be a violation of the prohibition to use EFPs for the sole purpose of circumventing the contract month roll.