CIRCULAR 053-21
March 22, 2021

REQUEST FOR COMMENTS

AMENDMENTS TO THE RULES OF BOURSE DE MONTREAL INC. CONCERNING TRADING HALTS ON EQUITY INDEX FUTURES

On March 16, 2021, the Rules and Policies Committee of Bourse de Montréal Inc. (the "**Bourse"**) approved amendments to the Rules of the Bourse in order to modify the rules pertaining to trading halts for certain index futures. The Bourse further proposes to modify the overnight trading range applicable to its index futures.

Comments on the proposed amendments must be submitted at the latest on **April 23, 2021**. Please submit your comments to:

Alexandre Normandeau
Legal Counsel
Bourse de Montréal Inc.
1800-1190 av des Canadiens-de-Montréal
P.O. Box 37
Montreal, Quebec H3B 0G7
E-mail: legal@tmx.com

A copy of these comments shall also be forwarded to the *Autorité des marchés financiers* (the "**Autorité**") to:

M[e] Philippe Lebel
Corporate Secretary and
Executive Director, Legal Affairs
Autorité des marchés financiers
Place de la Cité, tour Cominar
2640 Laurier boulevard, suite 400
Québec (Québec) G1V 5C1
Fax : (514) 864-8381
E-mail: consultation-en-cours@lautorite.qc.ca

Please note that comments received by one of these recipients will be transferred to the other recipient and that the Bourse may publish a summary of such comments as part of the self-certification process concerning this file. Unless specified otherwise, comments will be published anonymously by the Bourse.

Appendices

You will find in the appendices an analysis as well as the text of the proposed amendments. The implementation date of the proposed amendments will be determined by the Bourse, in accordance with the self-certification process as established by the *Derivatives Act* (CQLR, chapter I-14.01).

Process for Changes to the Rules

The Bourse is authorized to carry on business as an exchange and is recognized as a self-regulatory organization by the Autorité. The Board of Directors of the Bourse has delegated to the Rules and Policies Committee of the Bourse its powers to approve and amend the Rules, the Policies and the Procedures, which are thereafter submitted to the Autorité in accordance with the self-certification process as determined by the *Derivatives Act* (CQLR, chapter I-14.01).

AMENDMENTS TO THE RULES OF BOURSE DE MONTREAL INC. CONCERNING TRADING HALTS ON EQUITY INDEX FUTURES

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I. DESCRIPTION

Bourse de Montreal (the “Bourse”) proposes to modify certain index futures trading halt Rules as well as the trading range applicable to its index futures to ensure they are aligned with amendments the Chicago Mercantile Exchange (“CME”) implemented on October 12, 2020 (Overnight price limits) for its equity index futures. In Canada, although the Investment Industry Regulatory Organization of Canada (“IIROC”) is responsible for managing market-wide circuit breakers, these circuit breakers are triggered based on changes in the value of the S&P 500 Index. Therefore, the Bourse’s Rules necessitate modification in order to be aligned with the changes implemented in 2020 by the CME.

II. PROPOSED AMENDMENTS

The proposed amendments are attached.

Articles 12.506 and 12.606 are modified to allow the S&P/TSX 60 Index Standard Futures (SXF) and S&P/TSX 60 Index Mini Futures (SXM) to resume trading 5 minutes before the resumption of trading on the Underlying Interest S&P/TSX 60.

Article 6.210 is modified to clarify that no adjustments will be made to trades taking place when trading on the underlying interest of an equity index future is halted.

Note: All equity index futures contracts specification pages will also be modified to increase the overnight trading range from 5% to 7%. Such trading range is not part of the rules of the Bourse, but such modification is in line with the changes implemented in 2020 by the CME.

III. ANALYSIS

a. Background

The U.S. Securities and Exchange Commission mandated the creation of market-wide circuit breakers to prevent a repeat of the Oct. 19, 1987, market crash, when the Dow plunged 22.6%. Current guidelines mandate a 15-minute market-wide pause in all U.S. stocks if the S&P 500 index falls more than 7% before 3:25 p.m. New York time. Another circuit breaker is triggered if the index’s decline hits 13% before 3:25 p.m., and trading is suspended for the session if the drop reaches 20%.

The coordinated cross-market trading halts provided by circuit breaker procedures are designed to operate only during significant market declines and to substitute orderly, preplanned halts for the *ad hoc* and destabilizing halts that can occur when market liquidity is exhausted. The circuit breakers also protect investors and the markets by providing opportunities for markets and market participants to assess market conditions and potential systemic stress during a historic market decline.

Effective October 12, 2020, the CME amended its rules surrounding resumption of trading following regulatory halts on some of its Equity futures contracts (S&P500, E-minis, Dividend Index, Nasdaq 100).

During the regular trading session (9h30-15h25 ET), the corresponding 7% Price Limit shall apply until such time as the Primary Listing Exchange may declare a Regulatory Halt (Rule 35100.C[1].) in response to a Level 1 (7%) Market Decline in the S&P 500 Index, at which time futures trading shall halt. Futures trading shall resume 10 minutes after the Regulatory Halt commences on the Primary Listing Exchange, subject to the corresponding 13% Price Limit. At such time as the Primary Listing Exchange may declare a Regulatory Halt in response to a Level 2 (13%) Market Decline in the S&P 500 Index, futures trading shall halt. Futures trading shall resume 10 minutes after the Regulatory Halt commences on the Primary Listing Exchange. A 20% decline (Level 3 circuit breaker) in the S&P 500 Index will terminate trading for the remainder of the trading day in both the cash equity market and for all US-based Equity Index futures and options. From 15H25 to 16h00 ET., trading in futures for a given delivery month shall be subject only to the corresponding 20% Price Limit.

CME Equity index futures not included in the aforementioned changes would continue to resume trading when the Primary Exchange resumes trading which is 15 minutes after the halt is declared.

On that date, the CME also amended its rules concerning Equity Futures price limit ranges during the Overnight Trading Session ("OTH"). The CME modified the OTH Price Limits for equity futures from the previous 5% hard limits to 7% hard limits.

From 18h00 to 9h30 ET, there is a hard upside and downside limit of 7%. The midpoint of the 7% limit is based on the 16h00 futures fixing price. The width of the 7% limit is based on 7% of the underlying index value at 16h00. If markets reach 7% up or down during the overnight session, they remain open but can only trade up to those price limits.

b. Objectives

Since 2013, Canada's circuit breaker rules have been aligned with the ones employed by the United States (IIROC trading halts[2]). Therefore, recent changes to overnight price limits and trading halts brought forward by the CME on several of its Index Futures (S&P500, e-Minis) warrant corresponding amendments to the Bourse's equity index futures contracts. The following changes will be put in place:

1. Increase the trading range from 5% to 7% on all equity index futures. Such modification does not require changes to the Rules of the bourse.

2. Allow equity index futures contracts to resume trading 5 minutes before underlying index during regular trading session (10 mins v. 15 mins) on the following products:

    a. S&P TSX 60 Index Futures (SXF)
    b. S&P TSX 60 Index Mini Futures (SXM)

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[1] https://www.cmegroup.com/content/dam/cmegroup/rulebook/CME/IV/350/351/351.pdf

[2] https://www.iiroc.ca/Documents/2013/3a1b28bf-e586-479b-b2ea-bfcac791944b_en.pdf

Trading hours

Early or Overnight* session 2:00 a.m. to 9:15 a.m. ET

Regular session 9:30 a.m. to 4:30 p.m. ET

** Please keep in mind that once the Asian Trading Hours are in effect, the overnight session will start at 8:00pm ET (t-1)[3].*

c. Comparative Analysis

Rule 9.1 of UMIR[4] allows IIROC to impose a trading halt or suspension for regulatory purposes. As mentioned previously, the rule was updated on April 8, 2013, to align Canadian rules regarding general regulatory halts in the trading of securities with market-wide "circuit breakers" on markets in the United States.

This Rule imposes a general regulatory halt to be triggered when the S&P 500 Index or the S&P/TSX Composite Index, on a trading day or a portion of a trading day when U.S. markets are not scheduled to be open for trading, declines below its closing value on the previous trading day by:

Level 1 - 7%
Level 2 - 13%
Level 3 - 20%

Given the Bourse's alignment on market-wide circuit breakers with the cash equities market, it is judicious to follow suit for Canadian equity index futures when amendments are brought forth by U.S. peers concerning price limits and trading halt policies. Note: Equity price limits are downside limits during regular trading hours, with proposed hard upside and downside limits of 7% (current 5%) during overnight trading hours.

Several Asian markets have circuit breakers in place. In China, if the index known as the CSI 300 drops or rises 5 percent, it triggers a 15-minute halt, and after a 7 percent loss or gain, trading is shut down for the day. South Korea pauses trading for 20 minutes if its Kospi or Kosdaq indices lose 10 percent. India has a three-tiered system in place at 10, 15 and 20 percent above or below the last closing trading for the day before.

Interestingly, Japan doesn't have any circuit breakers in place for regular stock trading, but does halt trading on futures and options contracts if they reach upper or lower price limits.

In Europe, there are no market-wide circuit breakers like you'd find in the U.S. and Asia, but there are circuit breakers in place to prevent steep losses in individual stocks. On the London Stock Exchange (LSE), for example, individual stocks included in the benchmark FTSE100 index are protected by circuit breakers if trading drops 8 percent above or below the stock's opening price.

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[3] https://m-x.ca/f_circulaires_en/024-21_en.pdf

[4] https://www.iiroc.ca/industry/rulebook/Documents/UMIR0901_en.pdf

Similarly, Euronext will halt trading for three minutes on an individual stock if its price drops or rises too quickly below or above certain thresholds.

d. Analysis of Impacts

i. Impacts on Market

Opportunities:

1) Price discovery reinforcement of the futures contracts prior to the reopening of the cash market. A request by Market Makers[5] in the United States led to the CME trading halt rule amendments.

2) Improve the transition from the trading range in effect in the Overnight hours to the Regular trading hours.

Benefits:

1) Maintain consistency throughout North American derivatives exchanges in applying the same trading halt mechanisms and price limit/trading ranges for its equity index futures instruments.

2) Responding to client feedback quickly and attentively to avoid any disruptions and inconsistencies in procedural interpretation. Market participants have been leading catalysts in getting the Bourse to adopt the CME rule modifications in a quick and decisive manner.

ii. Impacts on Technology

Impacts should be minimal as monitoring procedures are already well established for trading ranges and trading halt protocols. Procedures and processes will have to be updated in order to program the expanded overnight trading range.

The proposed changes will require configuration modifications to take into account the increased trading range percentage.

iii. Impacts on regulatory functions

The proposed changes should have no impacts on the activities of the Regulatory Division of the Bourse.

iv. Impacts on clearing functions

The proposed changes should have no impacts on the activities of the Canadian Derivatives Clearing corporation (CDCC).

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[5] https://www.optiver.com/insights/news-articles/market-wide-circuit-breakers/

v. Public Interest

The Bourse is of the view that the proposed amendments are not contrary to the public interest. Market participants will appreciate the consistency in applying similar safeguard standards throughout North American marketplaces that are meant to protect investors when a market moves too far or too fast over a specific period of time.

IV. PROCESS

The proposed amendments, including this analysis, must be approved by the Bourse's Rules and Policies Committee and submitted to the Autorité des marchés financiers, in accordance with the self-certification process, and to the Ontario Securities Commission for information purposes.

V. ATTACHED DOCUMENTS

Proposed amendments to the rules.

Article 6.210 Trade Cancellation and or Price Adjustment

[…]

(h) No-Review Range. The Bourse will determine the limits of the No-Review Range by determining what was the acceptable market price for the Derivative Instrument before the Trade under review occurred based upon all relevant information, including the last Trade price, a better bid or offer, a more recent price for a related Derivative Instrument (for example a different expiry month) and the prices of similar Derivative Instruments trading on other markets once the acceptable market price is established, the Bourse applies the following increments to determine the limits of the No-Review Range;

DERIVATIVE INSTRUMENT	INCREMENT
[…]	
Futures Contracts on S&P/TSX and S&P/MX Indices and on the FTSE Emerging Markets Index - Regular strategy orders and Basis Trade on Close	1% of the acceptable market price of these Futures Contracts 5% of the increments for the outright month On such Futures Contracts, no adjustment will be made if the trade price is within 1 full index point of the acceptable market price or if the underlying index is subject to a trading halt
[…]	

[…]

Article 12.506 Trading Halts

(a) Trading halts shall be coordinated with the triggering of the trading halt mechanism of the Underlying Interest (circuit breakers).

(b) ~~In the event~~Provided that trading in the securities market is planned to resume~~s~~ after a 15 minutes trading halt, trading in the S&P/TSX 60 Index standard Futures shall resume ~~only~~ after a 10 minutes halt~~percentage (as determined by the Bourse from time to time) of the Underlying Interest S&P/TSX 60 Index have reopened~~.

[…]

Article 12.606 Trading Halts

(a) Trading halts shall be coordinated with the triggering of the trading halt mechanism of the Underlying Interest (circuit breaker).

(b) ~~In the event~~Provided that trading in the securities market is planned to resume~~s~~ after a 15 minutes trading halt, trading in the S&P/TSX 60 Index mini Futures shall resume ~~only~~ after a 10 minutes halt~~percentage (as determined by the Bourse from time to time) of the interest underlying the S&P/TSX 60 Index have re-opened~~.

[…]

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Article 6.210 Trade Cancellation and or Price Adjustment

[…]

(h) No-Review Range. The Bourse will determine the limits of the No-Review Range by determining what was the acceptable market price for the Derivative Instrument before the Trade under review occurred based upon all relevant information, including the last Trade price, a better bid or offer, a more recent price for a related Derivative Instrument (for example a different expiry month) and the prices of similar Derivative Instruments trading on other markets once the acceptable market price is established, the Bourse applies the following increments to determine the limits of the No-Review Range;

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