Bourse de Montréal Inc.

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

CIRCULAR
May 15, 2008

REQUEST FOR COMMENTS

RISKLESS BASIS CROSS TRANSACTIONS ON INDEX (SXF) AND SECTORIAL INDEX FUTURES CONTRACTS (SXA, SXB, SXH and SXY)

AMENDMENTS TO ARTICLES 6005 AND 6380 OF THE RULES OF THE BOURSE

Summary

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved amendments to articles 6005 and 6380 of the Rules of the Bourse, which deal with riskless basis cross transactions on Index (SXF) and Sectorial Index futures contracts (SXA, SXB, SXH and SXY). The main purpose of these amendments is to permit the implementation of a new trading mechanism in the equity index futures contracts that will allow the execution of riskless basis cross transactions and to clarify and distinguish certain concepts for the purpose of harmonizing the procedures and practices of the Bourse.

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 supervision responsibilities of 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.: 075-2008

The Division is under the authority of a Special Committee appointed by the Board of Directors of the Bourse. The Special Committee is empowered to recommend to the Board of Directors the approval or amendment of some aspects of the Rules and Policies of the Bourse governing approved participants, among which, the Rules and Policies relating to margin and capital requirements. The Board of Directors has delegated to the Rules and Policies Committee of the Bourse its powers to approve or amend these Rules and Policies with recommendation from the Special Committee. These changes are submitted to the Autorité for approval.

Comments on the proposed amendments to articles 6005 and 6380 of the Rules 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

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, 22nd Floor
P.O. Box 246, Tour de la Bourse
Montréal (Quebec) H4Z 1G3
E-mail: 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".

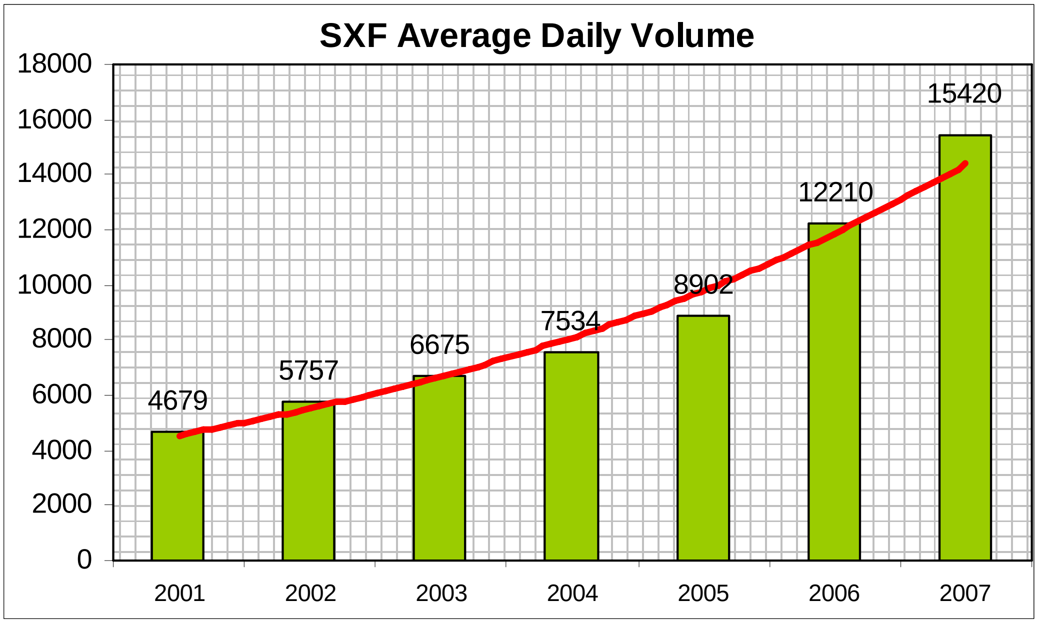
Bourse de Montréal Inc.

RISKLESS BASIS CROSS TRANSACTIONS ON INDEX (SXF) AND SECTORIAL INDEX FUTURES CONTRACTS (SXA, SXB, SXH and SXY)

AMENDMENTS TO ARTICLES 6005 AND 6380 OF THE RULES OF THE BOURSE

I. OVERVIEW

The S&P Canada 60 index futures contract (SXF) market has grown considerably since 2001.



The S&P Canada 60 stock index futures contract (SXF™) ***average daily volume of 15,420 contracts in 2007 is up 26% over 2006 and has more than tripled since 2001.***

The increase in market volumes has been fueled by a wider and more intensive use of the SXF futures contracts among end-users, and this in turn has led to a demand for a riskless basis cross facility. This facility would permit market participants to execute riskless trades of index futures contracts against cash instruments. Bourse de Montréal Inc. (the Bourse) proposes to implement this facility not only for the SXF futures contract but for the whole complex of equity index futures contracts, including the sectorial index futures contracts (SXA™, SXB™, SXH™ and SXY™). The proposed facility would offer more trading opportunities to users of index futures contracts and would enhance the performance of the sectorial index futures contracts.

II. RATIONALE

A. Market Interest Expressed

Market participants have asked for a facility that will permit them to buy/sell index futures contracts against cash instruments for an average cash market price plus a pre-negotiated basis spread. This request comes from approved participants who have received demands from their clients wishing to acquire market exposure in the most efficient way possible (often in the cash or Exchange Traded Fund (ETF) market) but not wanting (or being unable) to hold cash securities in their accounts. These clients are typically large institutional investors such as hedge funds, Commodity Trading Advisors (CTA) and asset managers. While average daily volumes traded have increased dramatically in the case of the SXF futures contract, the average trade size and the liquidity available in the Bourse's index futures contracts market is not adequate for the acquisition of institutional positions without causing market disruption. Average transaction size in the SXF is less than 2 contracts. This is clearly insufficient for the efficient acquisition of positions responding to institutional clients' needs (see Appendix I for an analysis of the SXF futures contract transaction size). The riskless basis trade would allow approved participants to take advantage of the liquidity of the cash market for their clients' benefit, and then cross the matching futures contracts positions into the client's account.

The riskless basis trade is a transaction where an approved participant and a client engage in prenegotiation discussions to agree upon the terms of an index futures contracts transaction to take place outside the Bourse's electronic trading system. This trade must include the acquisition by the approved participant of a position in the cash market. The terms agreed upon by the approved participant and its client also include the amount of exposure to the index required and the basis spread between the average price of the cash exposure acquired by the approved participant and the index futures contracts that will be crossed to the client.

To begin the operation, the approved participant will take a position (long/short) in cash instruments in its own account on behalf of the client. The approved participant will then execute the riskless basis cross trade on the index futures contracts, recording in its books a futures contracts position that offsets the cash position. The other side (position) of the futures contracts transaction will be allocated into the client's account, representing the amount of market exposure requested by the client. At the conclusion of the transaction, the approved participant's net position will be riskless, consisting of long (short) cash and short (long) futures contracts of equal value. The client will have the market exposure agreed upon in the form of futures contracts.

B. Riskless Basis Trades not Accommodated by the Bourse's Current Rules and Procedures

The current procedures regarding Exchange for Physical (EFP) transactions, prearranged and cross transactions as well as Block Trades do not accommodate the proposed type of operation.

- Riskless basis cross transactions do not fall under the EFP procedures because there is no exchange of a cash instrument for a futures contract between both parties.
- Current article 6380 of the Bourse's Rules and the applicable procedures for cross transactions and prearranged transactions are not adapted to the riskless basis cross transaction because this type of transaction does not have to be priced within the posted market (bid and ask) or the daily high and low.
- Riskless basis cross transactions do not fall under the procedures relative to block trades because a block trade requires a minimum quantity threshold to be executed and must be reported by the approved participant to the Market Operations Department of the Bourse within a maximum delay of 15 minutes after its execution. In addition a Block Trade does not require a related transaction in the cash market.

- Article 6005 of the Rules of the Bourse does not currently include riskless basis cross transactions in the list of off-exchange transactions that are permitted by the Bourse. This article would therefore need to be amended to include this type of transaction as a permissible off-exchange transaction.

In response to this demand from market participants, the Bourse proposes to implement new procedures that will allow the execution of riskless basis cross transactions on the SXF, SXA, SXB, SXH and SXY futures contracts.

C. Harmonization of the domestic cash and derivatives equity index markets

The Toronto Stock Exchange (TSX) has permitted this type of transaction (called Basis Trade) in the cash equity index market since 2003. TSX Policy 4-107 (*Specialty Price Crosses*) permits the execution of Basis Trades that comprise at least 80 percent of the component share weighting of the basket of securities or index participation unit that is the subject of the basis trade. Please see Appendix II for the relevant excerpts from the TSX Rule Book and Policies. The implementation by the Bourse of a riskless basis cross would mirror the TSX facility, and would require the same 80 percent weighting of the basket of securities or index participation units. The use of the same weighting requirement for the TSX basis trades and the Bourse's riskless basis cross transactions is important for the harmonization and efficiency of the cash and derivatives index market in Canada. The 80 percent weighting threshold can be explained by the fact that some institutional clients are not permitted to hold certain individual securities in the index. This 80 percent threshold provides a high degree of correlation while allowing the flexibility required for the exclusion of certain individual names.

III. DETAILED ANALYSIS

A. Riskless Nature of the Transaction

The Bourse would allow the use of a riskless basis cross facility to trade the SXF, SXA, SXB, SXH, and SXY futures contracts, provided that the approved participant's final position is riskless and therefore will not impact the cash market. Thus, a long (short) position in the underlying basket of equities would be offset by a short (long) position in the SXF, SXA, SXB, SXH or SXY futures contract. The risk offsetting features of this transaction would transform the net position of the approved participant into the equivalent of a short-term money market instrument maturing at the expiration of the futures contract. Please see Appendix III for a more complete explanation of the riskless nature of the approved participant's position.

The provisions that (1) exposure is acquired at an average cash market price and (2) the riskless nature of the position on the approved participant's books ensure that these trades will not disrupt or displace the exchange traded markets.

While the approved participant must acquire the cash market position before executing the futures contract leg, the Bourse will not impose any time limit for the retention or liquidation by the approved participant of the cash market position. Once the riskless basis cross has been completed, the approved participant may manage the positions on its books as it sees fit. This will further harmonize the transaction with the TSX Basis Trade facility, which similarly does not impose any retention or liquidation requirements.

B. Price of the Futures Contracts Transaction Firmly Anchored in the Cash Markets

The price that the client pays for index futures contracts has two components: the cash market average price and the basis. This price is obtained in the following manner:

1. Basis: The client and the broker agree on the basis that the client will pay above and beyond the cash market average price. This basis is negotiated between the broker and the client.

2. The client and the broker agree on the time period during which the broker will acquire exposure to the index. The average price of the cash instruments is calculated for that period.

3. The client's final price for the futures contracts is the average price of the cash market plus the prenegotiated basis.

The price of an index futures contract reflects very closely the price of the index on the cash market, with the difference between the two being the “basis” (Futures contract price= Cash price + Basis). While the price of the futures contracts transaction that forms part of the riskless basis cross may be outside the market posted on the Bourse’s electronic trading system, the acquisition of this exposure through transactions on the cash market firmly anchors the price of the transaction in the prevailing market.

As discussed above, the cash market exposure acquired by the approved participant must comprise of at least 80 percent of the component share weighting of the index underlying the futures contract that is the subject of the riskless basis cross. This provision exactly mirrors the provision in the TSX Rules and Policies for Basis Trades in the cash market.

C. Detailed Description of the Riskless Basis Cross

1. An approved participant receives an order from a client who wishes to acquire a given level of exposure to the S&P/TSX 60 index or to one of the S&P/TSX sectorial indexes (SXA, SXB, SXH or SXY). The client indicates that he does not want (or cannot) hold cash securities in his account.

2. The approved participant agrees to execute a transaction corresponding to the client’s needs for an average price in the cash market plus a basis (spread).

3. The approved participant starts acquiring cash market exposure (on its client’s behalf) purchasing cash instruments that the approved participant will accumulate and hold in its own account.

4. At the moment agreed between the approved participant and its client, the approved participant will execute a riskless basis cross exchanging a quantity of SXF, SXA, SXB, SXH or SXY futures contracts representing the total exposure requested by the client. The approved participant will hold in its books the index futures contracts offsetting the cash instruments and will allocate the other side of the riskless basis cross trade into the client's account.

5. The cash market exposure acquired by the approved participant must comprise at least 80 percent of the component share weighting of the index underlying the futures contract that is the subject of the riskless basis cross. This provision exactly mirrors the provision in the TSX Rules and Policies for Basis Trades in the cash market.

6. To be considered executed, the riskless basis cross transaction will have to be reported by the approved participant to the Market Operations Department of the Bourse by filling out and submitting through a specified Bourse’s website link a prescribed reporting form. Once the transaction has been registered by the Market Operations Department, the transaction will be marked and displayed at the trade recap level in the systems (trading platforms and data vendors) flagged by a special terms trading marker.

7. There will be no minimum time required to display (by the approved participant) the riskless basis cross transaction before its execution and the transaction will be recorded and reported without delay by the Market Operations Department of the Bourse.

8. A riskless basis cross transaction may only be executed during regular trading hours (same day as the order was submitted by the client) of the index futures contracts until 4:15 p.m.

9. There will be no minimum size restriction for this type of transaction.

10. There will be no requirement for the riskless basis cross transaction to be executed at a price that is within either the bid and ask or the daily high and low prices.

11. The riskless basis cross transaction will be excluded from the end of day settlement price procedures, but will be included in the daily volume figures.

12. The riskless basis cross transaction will appear in the Transaction Report maintained on the Bourse's Web page <http://www.m-x.ca/dailycrosses_en.php>.

IV. Proposed Amendment to Article 6005

Article 6005 enumerates those off-exchange transactions that are permitted by the Bourse. The riskless basis cross has the following characteristics that qualify it as an off-exchange transaction:

- pre-trade discussions
- the price of the transaction is determined outside the electronic trading system of the Bourse
- the transaction is reported to the Market Operations Department of the Bourse and manually validated and registered.

For the foregoing reasons the Bourse proposes to amend article 6005 by adding a new paragraph f) stipulating that the riskless basis cross is a permitted off-exchange transaction.

V. Proposed Amendments to Article 6380

Article 6380 applies to prenegotiation discussions, cross transactions, prearranged transactions and block trades.

A. Amendment to Paragraph 1) of Article 6380

The Bourse proposes to add the riskless basis cross transaction to the list of transactions that may result from prenegotiation discussions.

The Bourse would also take this opportunity to make some housekeeping amendments to this paragraph by adding references to Exchange for Risk (EFR) transactions for which amendments to article 6815 of the Rules were implemented on April 21, 2008.

B. Addition of a new Paragraph 5) to Article 6380

The Bourse proposes the addition of a new paragraph 5) to article 6380 to permit riskless basis cross transactions, consistent with the analysis and detailed description of this type of transaction as contained in this document.

The various conditions set in the proposed new paragraph are similar to those that are applicable to other types of transactions that are made outside of the electronic trading system of the Bourse such as exchange for physical transactions (EFP).

C. Deletion of subparagraph 3) iii) of article 6380

In addition to the modifications of article 6380 that are required for the riskless basis cross, the Bourse proposes to delete subparagraph 3) iii) of article 6380. This modification is intended to clarify the conditions under which a market participant can execute a cross or prearranged transaction directly in the Bourse's electronic trading system, as provided in article 6380 paragraph 3). Subparagraph 3) iii) of article 6380 as currently drafted stipulates that "Execution of cross transactions and prearranged transactions are permitted by the Bourse when: (…) iii) the transaction must be effected at a price that is at or between the current best bid and current best offer available in the electronic trading system of the Bourse;".

The Bourse proposes to delete this subparagraph because it is redundant in the context of the Bourse's electronic trading system's central limit order book, which respects strict price and time priority. Any order that is entered into the electronic trading system by a market participant must respect any marketable limit order that has been previously entered into the system. As a consequence, any cross transaction or prearranged transaction that is priced outside the best bid/offer and transacted in the electronic trading system of the Bourse will respect and fill all better bids (offers) that are resting in the book. Having filled all of the marketable limit orders in the book, the new order effectively becomes the best bid (offer) available in the electronic trading system of the Bourse. The integrity of the central limit order book is respected, and the client is filled at the best prices resting in the book before the balance of the order is crossed at the prenegotiated price.

For additional clarification, this modification only applies to those transactions contemplated in article 6380 paragraph 3); cross transactions and prearranged transactions that are entered into the electronic trading system directly by market participants. It does not apply to trades treated in other paragraphs of article 6380 such as block trades and riskless basis transactions both defined as Off-Exchange-Transactions (as per the provisions in article 6005) entered into the electronic trading system manually by the Market Operations Department. As per the nature of these special terms transactions, they are not required to respect the marketable limit orders resting in the central limit order book.

VI. OBJECTIVES

The proposed amendments to article 6380, relative to the execution of cross and pre-arranged transactions and of riskless basis transactions and to article 6005, relative to transactions outside of the order book are intended to permit the implementation of a new trading mechanism in the equity index futures contracts that will allow the execution of riskless basis cross transactions. In addition, the proposed amendments will permit to clarify and distinguish certain concepts (as described above) for the purpose of harmonizing the procedures and practices of the Bourse.

VII. IMPACT OF THE PROPOSED RULES AND PROCEDURES

The proposed amendments are mainly intended to integrate a new type of trading mechanism, as presented herein by the Bourse, called a riskless basis cross by allowing the execution of this type of transaction outside of the order book as defined by the related procedures.

The proposed amendment to article 6380 paragraph 3) will also allow the execution of pre-arranged transactions and cross transactions in the electronic trading system of the Bourse at prices that are outside of the best bid and offer while respecting the integrity of the central limit order book.

The Bourse believes that the proposed amendments will have no impact on systems for its approved participants.

VIII. PUBLIC INTEREST

The proposal to put in place a riskless basis cross transaction facility and to amend the Rules of the Bourse to allow for this type of transaction follows a demand for such a facility by market participants. Since this will result in a new trading mechanism, the Bourse considers that this proposal is of public interest. In addition, the introduction of this new proposed riskless basis cross mechanism will result in a more efficiently harmonized domestic equity index market for the best interest of the end users.

The proposed amendments will not contribute to the creation of an unfair discrimination between clients, issuers, brokers/dealers, approved participants or other persons. They will not impose any unnecessary or inappropriate competitive burden. The Bourse has also determined that the proposed amendments will not be detrimental to the interests of capital markets.

IX. PROCESS

The first step of the approval process for the regulatory amendments that are proposed in this analysis consists in having them approved by the the Rules and Policies Committee of the Bourse. Following such approval, a request for comments on the proposed amendments is then published by the Bourse by way of a circular.

The amendment proposal, including this analysis, is also transmitted to the Autorité des marchés financiers (AMF) for approval. The AMF also publishes a request for comments in its weekly Bulletin. The comment period ends 30 days after the publication date of the proposed amendments in the AMF weekly bulletin.

Finally, a copy of the proposed amendments is transmitted to the Ontario Securities Commission for information.

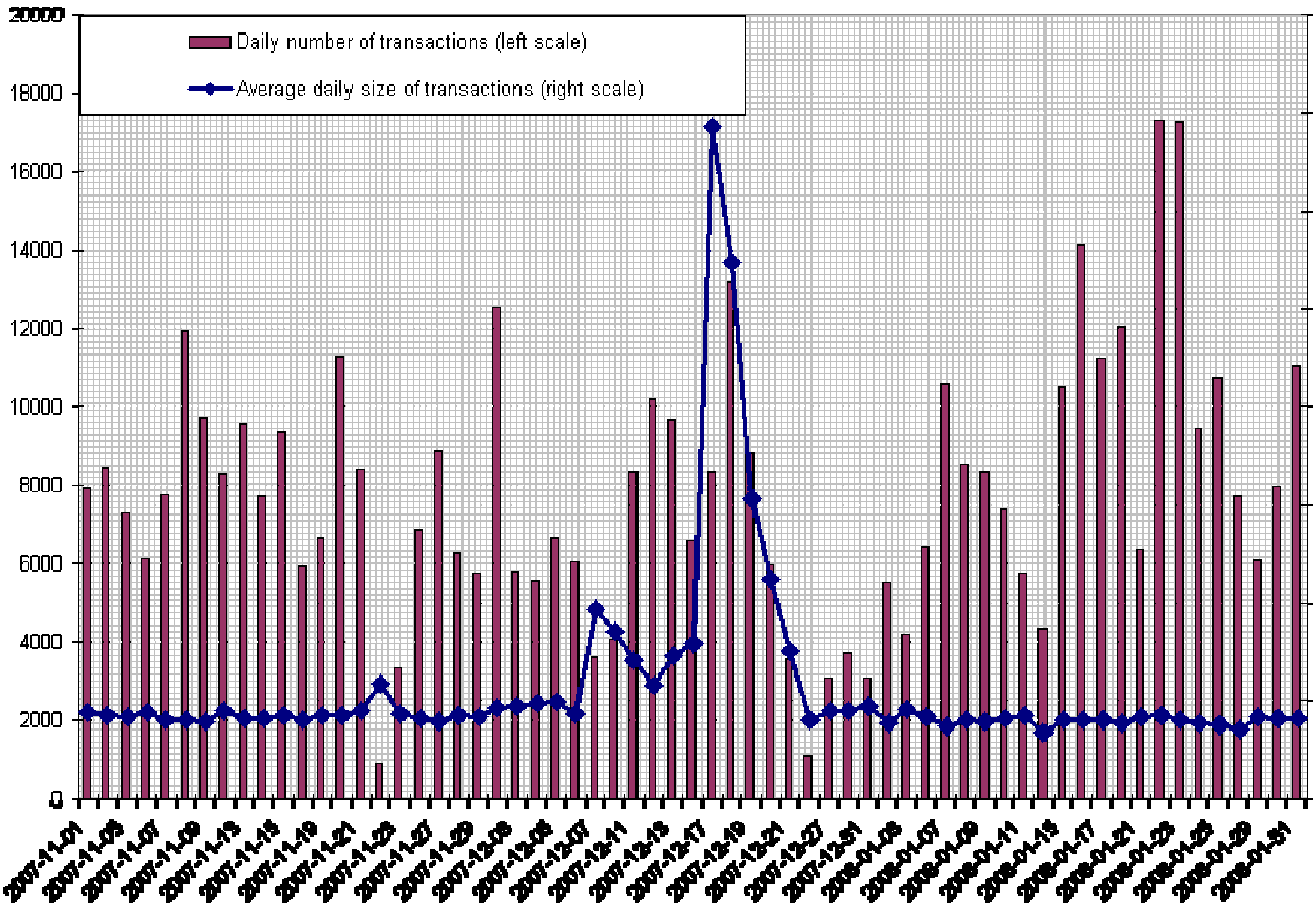
The management of the Bourse recommends that the Rules and Policies Committee approve the amendments to articles 6005 and 6380 of the Rules of the Bourse that are proposed in this document:

X. REFERENCE

- Rule Six of the Bourse: articles 6005 and 6380
- Rule 1-101 (Definitions) and Rule 4-107 (Specialty Price Crosses) of the Toronto Stock Exchange
- Policy 4-107 (Specialty Price Crosses) of the Toronto Stock Exchange

Appendix I

Liquidity of the SXF market
November 1, 2007 to January 31, 2008



- Based on a 3-month sample (Nov 2007. – Jan. 2008), we observe that the average size of a trade involving the S&P Canada 60 Index futures contract (SXF) is rarely higher than 2 contracts per trade. The average trade size of our sample is 2, while the average number of daily transactions is 7,803 transactions a day.

- This analysis demonstrates the need for a riskless basis cross transaction facility for institutional participants to make use of the liquidity of the cash markets to gain access to the futures contract market, and leads the Bourse to conclude that given the small size of SXF transactions (maximum of 2 contracts), a minimum threshold cannot be imposed to participants.

Appendix II

Excerpts from TSX Rule Book and Policies

- ## TSX Rule 1-101 Definitions (Amended)

"Basis Trade" means a transaction whereby a basket of securities or an index participation unit is transacted at a price calculated in the prescribed manner which represents the average accumulation (or distribution) price of the position, subject to an agreed upon basis spread, achieved through the execution of related exchange-traded derivative instruments, which may include listed index futures, index options and index participation units in an amount that will correspond to an equivalent market exposure.

Added (May 30, 2003)

- ## Rule 4-107 Specialty Price Crosses

(1) Execution
Specialty Price Crosses may be executed in the Regular Session and the Special Trading Session.

(2) Restriction on Setting Last Sale or Closing Price
Specialty Price Crosses shall not be used in the calculation of either a last sale price or closing price for a stock for the Regular Session or the Special Trading Session.

Added (May 30, 2003)

o **Policy 4-107 Specialty Price Crosses**

(1) <u>Qualifying Basis Trades</u>
A Basis Trade shall comprise of at least 80 percent of the component share weighting of the basket of securities or index participation unit that is the subject of the Basis Trade.

Appendix III

DEMONSTRATION THAT THE RISK OFFSETTING FEATURES OF A RISKLESS BASIS CROSS TRANSACTION WILL TRANSFORM THE NET POSITION OF THE APPROVED PARTICIPANT INTO THE EQUIVALENT OF A SHORT-TERM MONEY MARKET INSTRUMENT MATURING AT THE EXPIRATION OF THE FUTURES CONTRACT.

Money market:

The approved participant acquires money market exposure by purchasing a bond with a remaining maturity of 3 months at a discounted price of $99.50.

Value of the bond at maturity = « Par » = 100. The riskless rate *r* of the bond, for the holding period until maturity, is obtained from the following formula:

100 = 99.50 * (1+ r * T)

T = time to maturity = 3 months /12 = 0.25 year

Where r = 2.01% (Proof: 100 = 99.50*(1 + 0.0201*.25))

Replica portfolio consisting of a futures contract position and a cash position identical to the position held by the approved participant in the riskless basis transaction:

F = futures contract price, (780)

S = cash instrument price, (778)

T = time to expiry of the futures contract, (3 months)

r = risk free rate, (2.01% as calculated above)

d= dividend on the S&P/TSX 60 Canada index, (1.00%)

To replicate the riskless basis transaction we construct a portfolio consisting of a long position in the SXF futures contract and an equivalent short position in the cash market. The formula that relates the futures contract price (F) to the cash price (S) is:

F = S * (1+ (r – d) * T)

780 = 778 * (1+(r – 0.01)* 3 / 12) (Proof: 780 = 778* (1+(0.0201-0.01)*3/12)

Note: In reality the futures contract price (F) resulting from this calculation is 779.96445. Because the minimum price increment for the SXF is 0.10, we round F to 780.00

This calculation results in r = 2.01% (exactly as in the bond calculation above.)

Note: F=780 et S=778 are real prices obtained on March 25 2008 (source: Bloomberg)

Conclusion:

The replica portfolio position is riskless. The return is identical to the return on the bond because the risk free rates are equivalent. If the price of S increases by one dollar, the value of F also increases by one dollar. Therefore the riskless basis trade position, where the approved participant is long futures contract and short cash, remains neutral. The approved participant therefore has no directional exposure until the position expires, and the return *r* of this transaction is identical to the return on a money market instrument.

6005 Off-Exchange- Transactions
(10.10.91, 19.11.93, 14.07.95, 22.11.99, 21.04.08, 00.00.00)

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.

f) a riskless basis cross transaction in a security or derivative instrument designated by the Bourse and executed according to provisions of article 6380.

6380 Prenegotiation Discussions, Cross Transactions, Prearranged Transactions, and Block Trades and Riskless Basis Cross Transactions
(25.09.00, 24.09.01, 29.10.01, 31.01.05, 00.00.00)

For the purpose of this article, the terms hereunder are defined as follows:

1) Prenegotiation Discussions

Prenegotiation discussions are considered having occurred when approved participants engage in negotiations with each other or with other approved participants and/or clients prior to entering orders which may result in a cross transaction, a prearranged transaction, a block trade, ~~or~~ an exchange-for-physical or exchange-for-risk transaction (according to provisions of article 6815 of this Rule) or a riskless basis cross transaction. Clients must consent to allow approved participants to engage in prenegotiation discussions with other approved participants and/or clients with respect to an order.

2) Cross Transactions

A cross transaction is considered having occurred when two orders of opposite sides originating from the same approved participant are intentionally executed against each other in whole or in part as a result of prenegotiation discussions.

3) Prearranged Transactions

A prearranged transaction is considered having occurred when one or more approved participants engage in prenegotiation discussions in order to agree on the terms of a transaction before entering the orders in the electronic trading system of the Bourse.

Execution of cross transactions and prearranged transactions are permitted by the Bourse when:

i) they are on eligible securities or derivative instruments;

ii) the orders are for a quantity equal to or greater than the minimum quantity threshold established for that eligible security or derivative instrument;

~~iii) the transaction must be effected at a price that is at or between the current best bid and current best offer available in the electronic trading system of the Bourse;~~

iii~~v~~) the prescribed time delay between the input of an order and its opposite side order is respected in order to allow market participants to show their interest;

iv) the transactions are executed in accordance with the Procedures Applicable to the Execution of Cross Transactions and the Execution of Prearranged Transactions.

The eligible securities or derivative instruments, the prescribed time delays and the minimum quantity thresholds are determined by the Bourse and published in the Procedures Applicable to the Execution of Cross Transactions and the Execution of Prearranged Transactions.

It is forbidden to use the hidden quantity functionality of the electronic trading system of the Bourse to execute a cross transaction or a prearranged transaction.

4) Block Trades

A block trade is considered having occurred when one or more approved participants and/or clients engage in prenegotiation discussions to arrange large size transactions away from the electronic trading system of the Bourse (according to provisions of article 6005 of this Rule) at prices mutually agreed upon, report to the Bourse the terms of their agreement and the Bourse agrees to them.

An approved participant of the Bourse may execute a block trade for a quantity equal to or greater than the applicable minimum volume threshold in a security or derivative instrument, other than an equity option or a share futures contract, designated by the Bourse pursuant to the following conditions:

i) ~~a~~ A block trade may be arranged in a designated security or derivative instrument only during the trading hours and business days authorized by the Bourse. Once a block trade has been arranged, an approved participant must submit details of the block trade to the Bourse as soon as practicable and in any event within the period of time prescribed by the Bourse.

ii) A block trade may be arranged only in a security or derivative instrument that has been designated by the Bourse for that purpose. Such designations will be published by the Bourse, together with the minimum volume thresholds applying to those designated securities or derivative instruments. Approved participants are permitted to enter into block trades in any strategy recognized by the Bourse.

iii) Where a strategy involves the trading of two or more different securities or derivative instruments, the smaller of the minimum volume thresholds of the securities or derivative instruments comprised in the block trade will be applied to each of these securities or derivative instruments. Where the strategy involves the trading of two or more different contract months and/or strike prices of the same contract month, the minimum volume threshold will apply to each leg of the trade, except where specific provision has been made within the published minimum thresholds.

iv) Approved participants may not aggregate separate orders in order to meet the minimum volume thresholds.

v) The price at which a block trade is arranged must be "fair and reasonable" in light of (i) the size of such a block trade; (ii) currently traded prices and bid and ask prices in the same contract, at the relevant time; (iii) currently traded prices and bid and ask prices in other contract months for futures contracts or other option series for options contracts; (iv) currently traded prices and bid and ask prices in other relevant markets, including without limitation the underlying markets; (v) the volatility and liquidity of the relevant market; and (vi) general market conditions.

vi) Block trades shall not set off special term~~s~~ orders or otherwise affect orders in the regular market.

vii) It is strictly prohibited for an approved participant, for both the buyer and the seller, to enter into a block trade to circumvent the contract month roll in the corresponding security or derivative instrument.

The eligible securities or derivative instruments and the minimum quantity thresholds are determined by the Bourse and published in the Procedures for the Execution of Block Trades.

5) Riskless Basis Cross Transactions

A riskless basis cross transaction occurs when an approved participant and a client engage in pre negotiation discussions to conclude a riskless basis cross transaction outside of the posted order book (according to provisions of article 6005 of this Rule) at a pre-determined price. The index futures contract price is comprised of an~~the~~ average price~~,~~ resulting from a preliminary transaction in the cash market~~,~~ plus a prenegotiated basis spread mutually agreed upon between the approved participant and the client.

A riskless basis cross transaction can be executed on the Bourse once the approved participant has acquired market exposure using cash instruments as prescribed in the procedures established by the Bourse.

In order to qualify as a riskless basis cross transaction, the following conditions must be respected:

i) Riskless basis cross 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.

ii) The futures contracts that are eligible to riskless basis cross transactions, and the last day and time for executing such transactions shall be determined by the Bourse.

iii) The cash components acceptable for the purpose of a riskless basis cross transaction are those specified in the procedures set by the Bourse.

iv) Each party to a riskless basis cross transaction must satisfy the Bourse, upon request, that the transaction is a bona fide 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 and futures contracts and to any transfer of positions made in connection with such transaction.

v) It is prohibited for any party to a riskless basis cross 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~~trade", an accommodation trade or a fictitious sale.

vi) A riskless basis cross 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.

vii) Each riskless basis cross 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.

viii) Each riskless basis cross transaction must be immediately reported ~~to~~by the Bourse once it is executed.

ix) It is strictly prohibited for any party, for both the buyer and the seller, to enter into a riskless basis cross trade to circumvent the contract month roll in the corresponding security or derivative instrument.

PROCEDURES APPLICABLE TO THE EXECUTION OF RISKLESS BASIS CROSS TRANSACTIONS ON INDEX AND SECTORIAL INDEX FUTURES

Bourse de Montréal Inc. (the Bourse) authorizes riskless basis cross transactions on the S&P Canada 60 Index Futures contract (SXF™) or any of the listed sectorial index futures contracts (SXA™, SXB™, SXH™ and SXY™). The Bourse provides approved participants with a facility that permits the purchase/sale of index or sectorial futures contracts against cash instruments for an average cash market price plus a pre-negotiated basis. A riskless basis cross has no impact on the existing cash market as it results in a riskless transaction in the books of the approved participant. The offsetting feature of a riskless basis cross transaction transforms the approved participant's net position into the equivalent of a short-term money market instrument maturing at the expiration of the futures contract.

Approved participants receiving requests from clients who cannot or do not want to hold cash securities in their accounts but who wish to acquire market exposure in the most efficient way possible (often in the cash or exchange-traded fund "ETF" markets) are authorized to do a riskless basis cross. To begin the transaction, the approved participant is required to take position in cash instruments in its own account on behalf of the client. The approved participant then has to execute the riskless basis cross transaction (through the Bourse) and allocate the futures contract position, equivalent to the market exposure (as initially requested by the client) into the client's account.

Approved participants must apply the following procedures when executing riskless basis crosses:

- The approved participant agrees to execute a transaction on behalf of its client (who wishes to acquire equity index market exposure) for an average cash market price plus a pre-negotiated basis (spread).

- The approved participant begins by acquiring market exposure (long or short) on its client's behalf, using securities, baskets of securities, index participation units, or exchange-traded funds and accumulates them in its account.

- Once the cash transaction is completed, the approved participant executes a riskless basis cross transaction, at the time agreed with its client, for a predetermined quantity of index or sectorial index futures contracts. One side of this riskless basis cross transaction offsets the approved participant's position in the underlying cash market and the other side of the trade represents the total market exposure requested by the client. The resulting "unhedged" index futures contracts position is then allocated into the client's account.

- To execute the riskless basis cross transaction, the approved participant must provide the details of the concluded transaction to the Market Operations Department of the Bourse by filling out and submitting through the Bourse's Web page <http://www.m-x.ca/efp_formulaire_en.php> the prescribed "Contingent Trade Reporting Form". Once submitted, the riskless basis cross transaction will be registered by the Market Operations Department in the trading system. The transaction will then be specially marked and displayed in the systems (trading platform and data vendors) at the post trade recap level.

- Once concluded and registered, the riskless basis cross transaction will appear in the "Transaction Report" maintained on the Bourse's Web page <http://www.m-x.ca/dailycrosses_en.php>.

- A riskless basis cross transaction may only be executed during regular trading hours and no later than 4:15 p.m. on the day the approved participant received the order.

- There is no minimum time required to display (by the approved participant) the riskless basis cross transaction prior to execution. As soon as it is reported to the Market Operations Department at the Bourse, the transaction will be registered and displayed without delay.

- There is no minimum size restriction for a riskless basis cross transaction.

- There is no requirement for a riskless basis cross transaction to be executed within either the bid and ask or the daily high and low prices.

- The riskless basis cross transaction is excluded from the daily settlement price procedures, but is included in the daily volume figures.

- Approved participants involved in a basis cross transaction may be required to demonstrate to the Bourse:

    - that the cash market exposure acquired by the approved participant is comprised of at least 80 percent of the component share weighting of the index underlying the futures contract that is the subject of the riskless basis cross transaction; and
    - that the cash position and the futures contracts position (resulting from the riskless basis cross transaction) are properly recorded in both the approved participant's and client's accounts.

- While the approved participant must acquire the cash market position before executing the futures contract leg, the Bourse does not impose any time limit for the retention or liquidation by the approved participant of the cash market position. Once the riskless basis cross has been completed, the approved participant may manage the positions on its books as it sees fit.