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CIRCULAR
October 6, 2004

REQUEST FOR COMMENTS

MARGIN AND CAPITAL REQUIREMENTS FOR MONEY MARKET MUTUAL FUNDS

AMENDMENTS TO ARTICLE 7203

Summary

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved amendments to article 7203 of the Rules of the Bourse, which deal with margin and capital requirements for money market mutual funds. The purpose of these amendments is to establish a 5 percent margin rate requirement for positions in money market mutual funds held in approved participant accounts and client accounts.

Process for Changes to the Rules

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

Circular no.: 127-2004

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 article 7203 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".



MARGIN AND CAPITAL REQUIREMENTS FOR MONEY MARKET MUTUAL FUNDS

– AMENDMENTS TO ARTICLE 7203

I OVERVIEW

Bourse de Montréal Inc. (the “Bourse”) wishes to amend article 7203 of the Rules of the Bourse dealing with margin and capital requirements for money market mutual funds.

The proposed amendments aim to establish a 5% margin rate requirement for positions in money market mutual funds, as defined in National Instrument 81-102¹, held in approved participant accounts and client accounts.

II DETAILED ANALYSIS

A) Current Rules and The Issue

Under the current rules of the Bourse, for margin and capital requirements purposes, securities of mutual funds qualified by prospectus for sale in any province of Canada are treated on the same basis as listed stocks.

For money market mutual funds this requirement is deemed overly conservative, as the underlying securities to such funds are inherently less risky than equity securities. The Mutual Fund Dealers Association of Canada (the “MFDA”) rules recognize the lower risk

associated with money market mutual funds by assigning a 5% margin requirement to such funds. The result is that the current Bourse margin requirements for money market mutual funds are both overly conservative and inconsistent with those of the MFDA.

B) Objective

The objective of the proposed amendments to article 7203 of the Rules of the Bourse is to establish a 5% margin rate requirement for positions in money market mutual funds, as defined in National Instrument 81-102, held in approved participant accounts and client accounts.

C) Effect of Proposed Rules

Adoption of the proposed amendments will reduce costs, both in terms of capital usage and margin to be provided for approved participants and their clients respectively and will allow to harmonize the Bourse’s rules with MFDA’s rules.

D) Comparison with Similar Provisions

In arriving at the recommendation to reduce the margin and capital requirements for money market mutual funds, the margin rates for securities underlying these funds as well MFDA’s margin rate for money market mutual funds were considered.

E) Public Interest Objective

This proposal was designed to standardize industry practices for investor protection. The proposal does not permit unfair discrimination among customers, issuers, brokers, dealers, approved participants or others. It does not impose any burden on competition that is not necessary or appropriate in furtherance of the above purposes. Consequently, the proposed amendments are considered to be in the public interest.

¹ National Instrument 81-102 definition of “money market mutual fund” is presented as Attachment 1.

III COMMENTARIES

A) Effectiveness

The proposed amendments are believed to be effective in revising the required margin rate to more accurately reflect the risks associated with holding positions in money market funds and in conforming the requirements to that of the MFDA.

B) Process

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

IV REFERENCES

- Rule Seven of Bourse de Montréal Inc.;
- National Instrument 81-102, Mutual Funds;
- MFDA Financial Questionnaire and Report, Schedule 1 Notes and Instructions, Note 1(c).

NATIONAL INSTRUMENT 81-102
MUTUAL FUNDS

Part 1.1 – Definitions (extract)

“**money market fund**” means a mutual fund that has and intends to continue to have

- (a) all of its assets invested in any or all of
 - (i) cash,
 - (ii) cash equivalent,
 - (iii) evidences of indebtedness, other than cash equivalents, that have remaining terms to maturity of 365 days or less, or
 - (iv) floating rate evidences of indebtedness not referred to in subparagraph (ii) or (iii), if the principal amounts of the obligations will continue to have a market value of approximately par at the time of each change in the rate to be paid to the holders of the evidence of indebtedness,
 - (b) a portfolio with a dollar-weighted average term to maturity not exceeding 90 days, calculated on the basis that the term of a floating rate obligation is the period remaining to the date of the next rate setting,
 - (c) not less than 95 percent of its assets invested in cash, cash equivalents or evidences of indebtedness denominated in a currency in which the net asset value per security of the mutual fund is calculated, and
 - (d) not less than 95 percent of its assets invested in any or all of
 - (i) cash,
 - (ii) cash equivalents, or
 - (iii) evidences of indebtedness of issuers the commercial paper of which has an approved credit rating.
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7203 Unlisted Securities

(01.04.93, 18.02.00, 00.00.04)

a) ~~Securities unlisted on any exchange of the~~ The following unlisted securities types may be carried on margin on the same basis as prescribed for listed securities:

- ~~- securities of~~ Canadian banks;
 - ~~- securities of~~ insurance companies licensed to do business in Canada;
 - ~~- securities of~~ Canadian trust companies;
 - ~~— securities of mutual funds which are qualified for sale under prospectus in any province of Canada;~~
 - ~~- other~~ senior securities of already listed companies;
 - ~~-~~ unlisted securities in respect of which application ~~for listing has been approved by the Exchange, subject to fulfilling all of the requirements of the Exchange including distribution of these securities to a minimum number of public shareholders, or~~ has been made to list on a similarly approved by another recognized stock exchange in Canada and approval has been given subject to the filing of relevant documents and of satisfactory evidence of distribution; may be carried on margin for a period not exceeding 90 days from the date of ~~the conditional such approval or such other period as may be specified by the Exchange or another recognized stock exchange;~~
 - ~~- all eligible~~ securities which qualify as legal for investment by ~~the~~ Canadian life insurance companies, without recourse to the "basket clause";
- and
- ~~-~~ all securities listed on the Nasdaq Stock Marketsm (Nasdaq National Market® and The Nasdaq SmallCap Marketsm).

b) Where securities of mutual funds qualified by prospectus for sale in any province or territory of Canada are carried in a client or firm account, the margin required must be:

- i) 5% of the market value of the fund, where the fund is a money market mutual fund as defined in Part 1.1 of National Instrument 81-102 regarding mutual funds; or
- ii) the margin rate determined on the same basis as for listed stocks multiplied by the market value of the fund.

APPENDIX B

c) The minimum margin required on all other unlisted securities not mentioned above ~~unlisted on any exchange~~ must be as follows-

Long Positions

Margin Required

100% of market value

Short Positions

Credit Required

Securities trading at \$0.50 or more

200% of market value

Securities trading at less than \$0.50

Market value plus \$0.50 per share