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CIRCULAR 131-15
November 5, 2015

SELF-CERTIFICATION

MODIFICATIONS PERTAINING TO RISK MARGINING SYSTEMS

AMENDMENTS TO ARTICLES 9001 AND 9002 OF RULE NINE OF BOURSE DE MONTRÉAL INC.

The Rules and Policies Committee of Bourse de Montréal Inc. (the “Bourse”) has approved amendments to articles 9001 and 9002 of Rule Nine of the Bourse in order to recognize the role of the Canadian Derivatives Clearing Corporation (CDCC) in establishing the margin intervals used in risk margining systems, and to ensure that a uniform margin interval calculation is used for the calculation of customer margin and clearing house margin.

These amendments, as attached, were self-certified in accordance with the self-certification process as established in the *Derivatives Act* (CQLR, Chapter I-14.01) and will take effect on **November 30, 2015**. Please note that these articles will also be available on the Bourse’s website (www.m-x.ca).

The rule changes described in the present circular were published for public comment by the Bourse on June 3, 2015 (see [Circular 062-15](#)). Further to the publication of this circular, the Bourse has received comments. A summary of the comments received as well as responses from the Bourse to these comments is attached hereto.

For additional information, please contact Giancarlo Percio, Senior Analyst, Regulatory Division, at 514 787-6484 or at gpercio@m-x.ca.

Brian Z. Gelfand
Vice President and Chief Regulatory Officer

9001 Definitions

(01.01.05, 01.02.07, 30.11.15)

For the purpose of the present Rule:

- a) “**approved participant account**” means all non-client accounts including firm accounts, market maker accounts, restricted trading permit holder accounts for which a clearing approved participant has issued a letter of guarantee and sponsor accounts;
- b) “**client account**” means an account for a client of an approved participant, but does not include account in which a member of a self-regulatory organization, or a related firm, approved person or employee of such an approved participant, member or related firm, as the case may be, has a direct or indirect interest, other than an interest in a commission charged;
- c) “**escrow receipt**” means:
 - i) in the case of an equity, participation unit or bond option, a document issued by a financial institution approved by the Canadian Derivatives Clearing Corporation certifying that a security is held and will be delivered upon exercise by such financial institution in respect of a specified option of a particular client of an approved participant; or
 - ii) in the case of an OCC option, a document issued by a depository approved by the clearing corporation, after executing and delivering agreements required by The Options Clearing Corporation, certifying that a security is held and will be delivered upon exercise by such financial institution in respect of a specified OCC option of a particular client of an approved participant;
- d) “**firm account**” means an account established by an approved participant, which is confined to positions carried by the approved participant on its own behalf;
- e) “**floating margin rate**” means:
 - i) the last calculated regulatory margin interval, effective for the regular reset period or until a violation occurs, such rate to be reset on the regular reset date, to the calculated regulatory margin interval determined at that date; or
 - ii) where a violation has occurred, the last calculated regulatory margin interval determined at the date of the violation, effective for a minimum of twenty trading days, such rate to be reset at the close of the twentieth trading day, to the calculated regulatory margin interval determined at that date, where a reset results in a lower margin rate.

For the purposes of this definition, the term “regular reset date” is the date subsequent to the last reset date where the maximum number of trading days in the regular reset period has passed.

For the purposes of this definition, the term “regular reset period” is the normal period between margin rate resets. This period must be determined by the Canadian self-regulatory organizations with member regulation responsibilities and must not be no longer than sixty trading days.

For the purpose of this definition, the term “regulatory margin interval” means the margin interval calculated by the Canadian Derivatives Clearing Corporation. ~~when calculated, means the product of:~~

- ~~i) the maximum standard deviation of percentage changes in daily closing prices over the most recent 20, 90 and 260 trading days; and~~
- ~~ii) 3 (for a 99% confidence interval); and~~
- ~~iii) the square root of 2 (for two days coverage);~~
- ~~—rounded up to the next quarter percent.~~

For the purpose of this definition, the term "violation" means the circumstance where the maximum 1 or 2 day percentage change in the daily closing prices is greater than the margin rate;

- f) **“incremental basket margin rate”** means for a qualifying basket of index securities:
 - i) 100%, less the cumulative relative weight percentage (determined by calculating for each security the actual basket weighting in relation to the latest published relative weighting in the index and then determining an overall relative weight percentage) for the qualifying basket of index securities; multiplied by
 - ii) the weighted average margin rate for those equity securities comprising the basket for which the actual weighting is less than the latest published relative weight for the index (weighted by the percentage weighting deficiency for each security (i.e., the published relative weighting minus the actual weighting, if applicable));
- g) **"index"** means an equity index where:
 - i) the basket of equity securities underlying the index is comprised of eight or more securities;
 - ii) the weight of the single largest security position in the basket of equity securities underlying the index represents no more than 35% of the overall market value of the basket;
 - iii) the average market capitalization for each security position in the basket of equity securities underlying the index is at least \$50 million; and
 - iv) in the case of foreign equity indices, the index is both listed and traded on an exchange that meets the criteria for being considered a recognized exchange as set out in the definition of “regulated entities” included in the General Notes and Definitions to Policy C-3 of the Bourse;
- h) **“market maker account”** means a firm account of an approved participant that is confined to transactions initiated by a market maker;
- i) **“non-client account”** means an account established with an approved participant by another member of a self-regulatory organization, or related firm, approved person or employee of an approved participant, member or related firm, as the case may be, in which the approved participant does not have an interest, direct or indirect, other than an interest in fees or commissions charged;
- j) **“OCC option”** means a call option or a put option issued by The Options Clearing Corporation;

- k) “**participation unit**” means a unit of beneficial interest in the assets of a fund established under a trust agreement, the underlying asset of which are equities or other securities;
- l) “**qualifying basket of index securities**” means a basket of equity securities:
- i) all of which are included in the composition of the same index;
 - ii) which comprises a portfolio with a market value equal to the market value of the securities underlying the index;
 - iii) where the market value of each of the equity securities comprising the portfolio proportionally equals or exceeds the market value of its relative weight in the index, based on the latest published relative weights of securities comprising the index;
 - iv) where the required cumulative relative weighting percentage of all equity securities comprising the portfolio:
 - A) equals 100% of the cumulative weighting of the corresponding index, where the basket of equity securities underlying the index is comprised of less than twenty securities;
 - B) equals or exceeds 90% of the cumulative weighting of the corresponding index, where the basket of equity securities underlying the index is comprised of twenty or more securities but less than one hundred securities; and
 - C) equals or exceeds 80% of the cumulative weighting of the corresponding index, where the basket of equity securities underlying the index is comprised of one hundred or more securities;

based on the latest published relative weightings of the equity securities comprising the index;
 - v) where, in the circumstance where the cumulative relative weighting of all equity securities comprising the portfolio equals or exceeds the required cumulative relative weighting percentage and is less than 100% of the cumulative weighting of the corresponding index, the deficiency in the basket is filled by other equity securities included in the composition of the index;
- m) “**tracking error margin rate**” means the last calculated regulatory margin interval for the tracking error resulting from a particular offset strategy. The ~~method of calculation meaning of the term “regulatory margin interval”~~ and the margin rate policy ~~is are~~ the same as ~~that used~~ for the floating margin rate.

9002 Risk Margining Systems
(01.01.05, 30.11.15)

- a) With respect to an approved participant account constituted exclusively of positions in derivative instruments listed on the Bourse, the ~~capital margin~~ required may be the one calculated, ~~as the case may be,~~ by the Standard Portfolio Analysis (SPAN) methodology ~~or by the Theoretical Intermarket Margin System (TIMS) methodology,~~ using the margin interval calculated and the assumptions used by the Canadian Derivatives Clearing Corporation. ~~All changes to the assumptions used by the Canadian Derivatives Clearing Corporation must be approved by the Bourse prior to implementation~~

~~to ensure that the continued use of SPAN and TMS methodologies for regulatory purposes is appropriate.~~

~~The selected methodology (either SPAN or TMS) must be used consistently and cannot be changed without the prior consent of the Bourse. If the approved participant selects the SPAN methodology or the TMS methodology, the capital margin requirements calculated under these methodologies will supersede the provisions stipulated in the Rules.~~

~~For the purpose of the present article, “margin interval” means the product of the three following elements:~~

- ~~i) the maximum standard deviation of percentage fluctuations in daily settlement values over the most recent 20, 90 and 260 business days; multiplied by~~
 - ~~ii) 3 (for a 99% confidence interval); and multiplied by~~
 - ~~iii) the square root of 2 (for two days coverage).~~
- b) With respect to a client account, it is prohibited to use SPAN methodology ~~or TMS methodology~~ to determine margin requirements.

9001 Definitions

(01.01.05, 01.02.07, 30.11.15)

For the purpose of the present Rule:

- a) “**approved participant account**” means all non-client accounts including firm accounts, market maker accounts, restricted trading permit holder accounts for which a clearing approved participant has issued a letter of guarantee and sponsor accounts;
- b) “**client account**” means an account for a client of an approved participant, but does not include account in which a member of a self-regulatory organization, or a related firm, approved person or employee of such an approved participant, member or related firm, as the case may be, has a direct or indirect interest, other than an interest in a commission charged;
- c) “**escrow receipt**” means:
 - i) in the case of an equity, participation unit or bond option, a document issued by a financial institution approved by the Canadian Derivatives Clearing Corporation certifying that a security is held and will be delivered upon exercise by such financial institution in respect of a specified option of a particular client of an approved participant; or
 - ii) in the case of an OCC option, a document issued by a depository approved by the clearing corporation, after executing and delivering agreements required by The Options Clearing Corporation, certifying that a security is held and will be delivered upon exercise by such financial institution in respect of a specified OCC option of a particular client of an approved participant;
- d) “**firm account**” means an account established by an approved participant, which is confined to positions carried by the approved participant on its own behalf;
- e) “**floating margin rate**” means:
 - i) the last calculated regulatory margin interval, effective for the regular reset period or until a violation occurs, such rate to be reset on the regular reset date, to the calculated regulatory margin interval determined at that date; or
 - ii) where a violation has occurred, the last calculated regulatory margin interval determined at the date of the violation, effective for a minimum of twenty trading days, such rate to be reset at the close of the twentieth trading day, to the calculated regulatory margin interval determined at that date, where a reset results in a lower margin rate.

For the purposes of this definition, the term “regular reset date” is the date subsequent to the last reset date where the maximum number of trading days in the regular reset period has passed.

For the purposes of this definition, the term “regular reset period” is the normal period between margin rate resets. This period must be determined by the Canadian self-regulatory organizations with member regulation responsibilities and must not be no longer than sixty trading days.

For the purpose of this definition, the term “regulatory margin interval” means the margin interval calculated by the Canadian Derivatives Clearing Corporation.

For the purpose of this definition, the term "violation" means the circumstance where the maximum 1 or 2 day percentage change in the daily closing prices is greater than the margin rate;

- f) **"incremental basket margin rate"** means for a qualifying basket of index securities:
 - i) 100%, less the cumulative relative weight percentage (determined by calculating for each security the actual basket weighting in relation to the latest published relative weighting in the index and then determining an overall relative weight percentage) for the qualifying basket of index securities; multiplied by
 - ii) the weighted average margin rate for those equity securities comprising the basket for which the actual weighting is less than the latest published relative weight for the index (weighted by the percentage weighting deficiency for each security (i.e., the published relative weighting minus the actual weighting, if applicable));
- g) **"index"** means an equity index where:
 - i) the basket of equity securities underlying the index is comprised of eight or more securities;
 - ii) the weight of the single largest security position in the basket of equity securities underlying the index represents no more than 35% of the overall market value of the basket;
 - iii) the average market capitalization for each security position in the basket of equity securities underlying the index is at least \$50 million; and
 - iv) in the case of foreign equity indices, the index is both listed and traded on an exchange that meets the criteria for being considered a recognized exchange as set out in the definition of "regulated entities" included in the General Notes and Definitions to Policy C-3 of the Bourse;
- h) **"market maker account"** means a firm account of an approved participant that is confined to transactions initiated by a market maker;
- i) **"non-client account"** means an account established with an approved participant by another member of a self-regulatory organization, or related firm, approved person or employee of an approved participant, member or related firm, as the case may be, in which the approved participant does not have an interest, direct or indirect, other than an interest in fees or commissions charged;
- j) **"OCC option"** means a call option or a put option issued by The Options Clearing Corporation;
- k) **"participation unit"** means a unit of beneficial interest in the assets of a fund established under a trust agreement, the underlying asset of which are equities or other securities;
- l) **"qualifying basket of index securities"** means a basket of equity securities:
 - i) all of which are included in the composition of the same index;
 - ii) which comprises a portfolio with a market value equal to the market value of the securities underlying the index;

- iii) where the market value of each of the equity securities comprising the portfolio proportionally equals or exceeds the market value of its relative weight in the index, based on the latest published relative weights of securities comprising the index;
- iv) where the required cumulative relative weighting percentage of all equity securities comprising the portfolio:
 - A) equals 100% of the cumulative weighting of the corresponding index, where the basket of equity securities underlying the index is comprised of less than twenty securities;
 - B) equals or exceeds 90% of the cumulative weighting of the corresponding index, where the basket of equity securities underlying the index is comprised of twenty or more securities but less than one hundred securities; and
 - C) equals or exceeds 80% of the cumulative weighting of the corresponding index, where the basket of equity securities underlying the index is comprised of one hundred or more securities;

based on the latest published relative weightings of the equity securities comprising the index;

- v) where, in the circumstance where the cumulative relative weighting of all equity securities comprising the portfolio equals or exceeds the required cumulative relative weighting percentage and is less than 100% of the cumulative weighting of the corresponding index, the deficiency in the basket is filled by other equity securities included in the composition of the index;
- m) "**tracking error margin rate**" means the last calculated regulatory margin interval for the tracking error resulting from a particular offset strategy. The meaning of the term "regulatory margin interval" and the margin rate policy are the same as for the floating margin rate.

9002 Risk Margining Systems

(01.01.05, 30.11.15)

- a) With respect to an approved participant account constituted exclusively of positions in derivative instruments listed on the Bourse, the margin required may be the one calculated by the Standard Portfolio Analysis (SPAN) methodology using the margin interval calculated and the assumptions used by the Canadian Derivatives Clearing Corporation.

If the approved participant selects the SPAN methodology, the margin requirements calculated under this methodology will supersede the provisions stipulated in the Rules.

- b) With respect to a client account, it is prohibited to use SPAN methodology to determine margin requirements.

**MODIFICATIONS PERTAINING TO RISK MARGINING SYSTEMS
AMENDMENTS TO ARTICLES 9001 AND 9002**

**Summary of comments received following the publication of [Circular 062-15](#)
and responses from the Bourse**

Comments	Responses from the Bourse
<p>The Commenter agrees with the proposed rule amendments. It will result in a single margin interval for client and approved participant accounts. Along with other changes announced by the Canadian Derivatives Clearing Corporation, the proposed rule amendments will help bring the margining framework more in line with international best practices and ensure that margin requirements better reflect the risk of a portfolio.</p>	<p>The Bourse thanks the commenter for its time and its consideration of this matter.</p>