CIRCULAR 148-23
December 14, 2023

REQUEST FOR COMMENTS

AMENDMENTS TO THE RULES OF THE BOURSE REGARDING POSITION LIMITS ON GOVERNMENT OF CANADA BOND LISTED PRODUCTS

On December 1st, 2023, the Self-Regulatory Oversight Committee ("SROC") of Bourse de Montréal Inc. (the "Bourse") approved amendments of the Rules of the Bourse (the "Rules") regarding position limits on Government of Canada bond Listed Products.

Comments on the proposed amendments must be submitted at the latest on January 31st, 2024. Please submit your comments to:

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

Me 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 Division 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 Regulatory Division of the Bourse (the “Division”) is responsible for the regulatory functions of the Bourse and carries on its activities as an independent unit separate from the other activities of the Bourse. The Division’s activities are performed under the oversight of the SROC appointed by the Board of Directors of the Bourse.

New rule proposals or amendments to rules pertaining to market integrity (the "Market Integrity Rules") are vested with the Division. Any proposals and amendments to the Market Integrity Rules are presented to the Advisory Committee on Self-Regulation for recommendations before being submitted for SROC’s approval. The proposals and amendments 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 THE BOURSE REGARDING POSITION LIMITS ON GOVERNMENT OF CANADA BOND LISTED PRODUCTS

I. DESCRIPTION

Currently, the Rules establish a maximum net long or short position a Person may own or control in the delivery month at the close of trading on the first business day of the delivery month (a "Spot Month Position Limit") for Government of Canada Bond futures and options on Government of Canada Bond futures ("Government of Canada Bond Listed Products") pursuant to subparagraph 6.309B(b)(ii). The Division proposes to modify the Spot Month Position Limit on Government of Canada Bond Listed Products such that the Spot Month Position Limits are established and published earlier and such that the calculation is based on the cheapest issue eligible for delivery (the "Cheapest-to-Deliver").

II. OUTLINE OF THE AMENDMENTS

The Division proposes to amend subparagraph (b)(ii) of Article 6.309B (Position Limits for Futures Contracts) of the Rules to modify the Spot Month Position Limit on Government of Canada Bond Listed Products (the "Proposed Amendments").

The Proposed Amendments are attached as follows:

- Appendix A—Blackline version of the amendments
- Appendix B—Clean version of the amendments

III. ANALYSIS

a. Background

On February 12, 2015, the Bourse self-certified amendments instituting a spot month position limit on Government of Canada Bond Listed Products as the lesser of (i) 20% of the open interest of that contract month at the start of trading on the first business day prior to the first delivery notice day of the first contract month and (ii) the futures contract equivalent of 5% of the total outstanding amount of Government of Canada bonds eligible for delivery for the designated Government of Canada bond futures contracts at the start of trading on the first business day prior to the first delivery notice day of the first contract month.[1] Prior to those amendments, the Bourse solely relied on condition (i) for establishing Spot Month Position Limits. On February 4, 2016, the Bourse self-certified amendments to remove condition (i) and rely solely on condition (ii) to establish Spot Month Position Limits.[2]

To illustrate the current method, consider the Spot Month Position Limits of March 2023. On February 24, 2023, the Bourse published the bonds eligible for delivery.[3] For Ten-Year Government of Canada Bond Futures ("CGB") for the March 2023 contract ("CGBH23"), five different underlying bonds with a total outstanding amount of $127B were eligible for delivery. The Spot Month Position Limit, the futures contract equivalent to 5% of $127B, was established as 63,500 contracts and published on February 24, 2023, with an effective date of March 1, 2023 at the market close.[4]

The Division is of the opinion that the method for establishing and publishing Spot Month Position Limits on Government of Canada Bond Listed Products could be further improved in two different aspects. First, the position limits are currently published two to three business days prior to the effective date and

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[1] Circular 014-15
[2] Circular 018-16
[3] Appendix I of Circular 031-23
[4] Circular 032-23

therefore potentially creates market frictions. Second, the position limits are established based on the total outstanding amount of underlying bonds eligible for delivery and do not optimally reflect the fundamentals in which a Spot Month Position Limit is intended for. The Proposed Amendments will improve market efficiency and continue protecting the market from risks of market abuse.

b. Objectives

Position limits aim to prevent excessive speculation and manipulation while ensuring sufficient market liquidity for bona fide hedgers and protecting the price discovery process. Setting appropriate position limits is necessary, especially on Listed Products with physical settlement to ensure the open positions do not exceed the actual deliverable supply. The position limits on these Listed Products in turn ensure orderly pricing on the underlying interest and that no market participant corners the market. In the case of Government of Canada Bond futures, short position holders may deliver a variety of different underlying bonds that are eligible for delivery, but will choose to deliver the underlying bond issue that will minimize their costs in satisfying their delivery obligations. For example, five different underlying bond issues were eligible for delivery for CGBH23[5] and short position holders all delivered the bond issue with a coupon of 1.5% maturing in June 2030. Empirically, the Division notes short position holders systemically delivered the Cheapest-to-Deliver for all Government of Canada Bond futures over the period from March 2020 to September 2023. Therefore, the Division believes that a Spot Month Position Limit based on the Cheapest-to-Deliver rather than the entirety of the bond issues eligible for delivery is more appropriate in preventing any market cornering or price manipulation and maintaining orderly pricing on the underlying interest.

The Division believes that 15% of the outstanding amount of the Cheapest-to-Deliver is an appropriate proportion in establishing Spot Month Position Limits. In reaching such a conclusion, the Division considered comparisons with the previous Spot Month Position Limits and any breaches that would have resulted had the Proposed Amendments been in effect. The Division also considered a comparative analysis with other marketplaces and the details are set out in the next section.

The table hereunder illustrates the variation between a Spot Month Position Limit established as 5% of the total outstanding amount of bonds eligible for delivery (the "Current Method") and a Spot Month Position Limit established at 15% of the total outstanding amount of the Cheapest-to-Deliver (the "Proposed Method").

	Eligible Bonds	**Cheapest to Deliver**		**Spot Month Position Limit**		
Contract	**Outstanding Amount ($M)**		**Issue**	**Current Method**	**Proposed Method**	**Variation**
CGBH21	86,500	12,300	CAN 2 ¼ 06/01/29	43,250	18,450	-57%
CGBM21	107,500	12,300	CAN 2 ¼ 06/01/29	53,750	18,450	-66%
CGBU21	121,200	44,200	CAN 1 ¼ 06/01/30	60,600	66,300	9%
CGBZ21	135,200	44,200	CAN 1 ¼ 06/01/30	67,600	66,300	-2%
CGBH22	153,200	44,200	CAN 1 ¼ 06/01/30	76,600	66,300	-13%
CGBM22	175,200	44,200	CAN 1 ¼ 06/01/30	87,600	66,300	-24%
CGBU22	144,000	40,000	CAN 0 ½ 12/01/30	72,000	60,000	-17%

[5] Appendix I of Circular 031-23

Contract	Eligible Bonds	Cheapest to Deliver		Spot Month Position Limit		
	Outstanding Amount ($M)		Issue	Current Method	Proposed Method	Variation
CGBZ22	155,000	40,000	CAN 0 ½ 12/01/30	77,500	60,000	-23%
CGBH23	127,000	42,000	CAN 1 ½ 06/01/31	63,500	63,000	-1%
CGBM23	138,000	42,000	CAN 1 ½ 06/01/31	69,000	63,000	-9%
CGBU23	102,500	32,000	CAN 1 ½ 12/01/31	51,250	48,000	-6%
CGFH21	73,500	47,500	CAN 0 ½ 09/01/25	36,750	71,250	94%
CGFM21	42,000	34,000	CAN 0 ¼ 03/01/26	21,000	51,000	143%
CGFU21	53,500	34,000	CAN 0 ¼ 03/01/26	26,750	51,000	91%
CGFZ21	32,000	23,000	CAN 1 09/01/26	16,000	34,500	116%
CGFH22	40,000	23,000	CAN 1 09/01/26	20,000	34,500	73%
CGFM22	21,000	17,000	CAN 1 ¼ 03/01/27	10,500	25,500	143%
CGFU22	29,000	17,000	CAN 1 ¼ 03/01/27	14,500	25,500	76%
CGFZ22	23,500	16,000	CAN 2 ¾ 09/01/27	11,750	24,000	104%
CGFH23	27,500	16,000	CAN 2 ¾ 09/01/27	13,750	24,000	75%
CGFM23	30,000	15,000	CAN 3 ½ 03/01/28	10,000	22,500	125%
CGFU23	35,000	15,000	CAN 3 ½ 03/01/28	17,500	22,500	29%
CGZH21	146,100	37,000	CAN 0 ¼ 11/01/22	73,050	55,500	-24%
CGZM21	107,500	32,000	CAN 0 ¼ 02/01/23	53,750	48,000	-11%
CGZU21	99,000	30,000	CAN 0 ¼ 05/01/23	49,500	45,000	-9%
CGZZ21	80,500	20,000	CAN 0 ¼ 08/01/23	40,250	30,000	-25%
CGZH22	71,000	16,500	CAN 0 ½ 11/01/23	35,500	24,750	-30%
CGZM22	47,500	17,500	CAN 0 ¾ 02/01/24	23,750	26,250	11%
CGZU22	50,500	16,000	CAN 1 ½ 05/01/24	25,250	24,000	-5%
CGZZ22	52,000	16,500	CAN 2 ¾ 08/01/24	26,000	24,750	-5%
CGZH23	46,500	16,000	CAN 3 11/01/24	23,250	24,000	3%
CGZM23	57,000	15,000	CAN 3 ¾ 02/01/25	28,500	22,500	-21%
CGZU23	53,750	15,250	CAN 3 ¾ 05/01/25	26,875	22,875	-15%
LGBH21	54,710	14,900	CAN 2 ¾ 12/01/48	27,355	22,350	-18%
LGBM21	63,718	14,900	CAN 2 ¾ 12/01/48	31,859	22,350	-30%
LGBU21	72,718	14,900	CAN 2 ¾ 12/01/48	36,359	22,350	-39%
LGBZ21	64,818	51,817	CAN 2 12/01/51	32,409	77,726	140%
LGBH22	70,818	51,817	CAN 2 12/01/51	35,409	77,726	120%
LGBM22	74,818	51,817	CAN 2 12/01/51	37,409	77,726	108%
LGBU22	78,818	51,817	CAN 2 12/01/51	39,409	77,726	97%
LGBZ22	83,818	51,817	CAN 2 12/01/51	41,909	77,726	85%

Contract	Eligible Bonds	Cheapest to Deliver		Spot Month Position Limit		
	Outstanding Amount ($M)		Issue	Current Method	Proposed Method	Variation
LGBH23	83,818	51,817	CAN 2 12/01/51	41,909	77,726	85%
LGBM23	83,818	51,817	CAN 2 12/01/51	41,909	77,726	85%
LGBU23	38,750	6,750	CAN 2 ¾ 12/01/55	19,375	10,125	-48%

With regards to the publication of the Spot Month Position Limits, the current Rules specify that the Spot Month Position Limit is based on the total amount of outstanding bonds eligible for delivery “at market close on the fourth business day prior to the first business day of the first delivery month”. This specific language prevents the Division from publishing the Spot Month Position Limits prior to the fourth business day of the effective day. The Proposed Amendments abrogate the quoted text and therefore allows the publication of the Spot Month Position Limits at an earlier date and eliminates market frictions that may arise from late publications. With these Proposed Amendments, the Division preliminarily intends to publish the Spot Month Position Limits ten business days prior to the effective date.

The Division notes that the Cheapest-to-Deliver may change from time to time but does not expect such changes to be a challenge. Empirically, for the period from March 2020 to September 2023, the Division has not observed any changes in the Cheapest-to-Deliver that occurred between mid-month prior to a delivery month and the expiration of the contract.

c. Comparative Analysis

In a comparative analysis involving six different marketplaces, the Division notes that only the CBOT and ASX 24 apply spot month position limits on similar products.

Market-place	Products	Settlement	Spot Month Position Limits
CBOT	Eight different futures on treasury notes and bonds	Physical	Published at the close of the second business date of the month prior to a delivery month and effective during the last ten trading days of each product
ICE Futures Europe	16 different futures on short-, medium- or long-term debt instruments issued by the United Kingdom, Federal Republic of Germany, the Republic of Italy, the Kingdom of Spain or the Swiss Confederation	Physical	None
Eurex	11 different futures on short-, medium- and long-term debt instruments issued by the Federal Republic of Germany, the Republic of Italy, the Republic of France, the Kingdom of Spain or the Swiss Confederation	Physical	None

Market-place	Products	Settlement	Spot Month Position Limits
ASX 24	Futures on three-, five-, ten- and 20-year commonwealth treasury bonds	Cash	Fixed and effective during the last trading day of each product
HKEX	Futures on five-year China Ministry of Finance treasury bonds	Cash	None
Osaka Exchange	Futures on five- and ten-year Japanese government bonds and mini futures on 20-year Japanese government bonds	Physical	None
	Mini futures on ten-year Japanese government bonds	Cash	None

Although the Commodity Futures Trading Commission does not require spot month position limits on treasury note and bond futures, the CBOT nevertheless applies limits that have remained largely unchanged from September 2021 to September 2023. On August 10, 2023, these limits corresponded to an amount varying from 7.7% to 21.4% and a median of 16.4% of the total outstanding amount of the Cheapest-to-Deliver.

	Cheapest-to-Deliver		Initial Spot Month Limit	
CBOT Futures Product	Outstanding Amount ($M)	Issue	# of contracts	% of Cheapest-to-Deliver
2-Year T-Note	41,000	3 ½ 09/15/25	35,000	17.1%
3-Year T-Note	40,000	4 ⅛ 06/15/26	30,000	15.0%
5-Year T-Note	43,000	3 ⅞ 11/30/27	85,000	19.8%
10-Year T-Note	35,000	3 ¾ 05/31/30	75,000	21.4%
Ultra 10-Year U.S. Treasury Note	99,000	3 ⅜ 05/15/33	125,000	12.6%
U.S. Treasury Bond	39,000	4 ½ 08/15/39	30,000	7.7%
20-Year U.S. Treasury Bond	42,000	3 ⅞ 02/15/43	80,000	19.0%
Ultra U.S. Treasury Bond	51,000	3 02/15/49	80,000	15.7%

d. Analysis of Impacts

i. Impacts on Market

The Proposed Amendments relieve market participants from unwinding positions in the current two to three business days during an illiquid period of a roll and further set limits that more accurately reflect the risks associated with physical delivery. Consequently, the Division believes that the Proposed Amendments will improve market efficiency and continue protecting the market from risks of market abuse.

ii. Impacts on Technology

The Proposed Amendments have no impact on the technological systems of the Bourse, the Canadian Derivatives Clearing Corporation ("CDCC"), Approved Participants, independent software vendors, or any other market participant. The Division has not identified any impediments, whether technical, operational or other, to the implementation of the Proposed Amendments.

iii. Impacts on Regulatory Functions

The Proposed Amendments will not affect the Division's functions in relation to the monitoring, and enforcing spot month position limits on Government of Canada Bond Listed Products. The changes in establishing and publishing spot month position limits will not have a significant impact on the Division's operations.

iv. Impacts on Clearing Functions

The Proposed Amendments have no impact on the clearing functions of the CDCC.

v. Impacts on Compliance with Laws

The proposal has no impact on the compliance, supervision and reporting rules on the Bourse or the Division. Approved Participants must comply with the Rules and are subject to the oversight of the Division. Approved Participants must at all times adhere to the principles of good business practice in the conduct of their affairs.

vi. Public Interest

The Proposed Amendments will have a positive impact on the market and market participants as the Proposed Method to establish position limits will be more reflective of the fundamentals in which a Spot Month Position Limit is intended for. The publication process will also be more effective. The Proposed Amendments are further aligned with the endeavour of the Bourse and the Division to counter market abuse and manipulation, fraud and deceptive trading, and to foster fair and orderly trading which ultimately provide an efficient and transparent market. For these reasons, the Division considers that the Proposed Amendments are in the public interest.

APPENDIX A—BLACKLINED VERSION OF THE AMENDMENTS

Article 6.309B Position Limits for Futures Contracts

Except as otherwise indicated and except for Share Futures Contracts, the applicable position limits for Futures Contracts are as follows:

[...]

(b) Government of Canada Bond Futures:

(i) For all expiration months combined for each designated Government of Canada Bond Futures Contract, the maximum net Long Position or net Short Position which a Person may own or control at the close of trading on the first business day of the month following the Delivery Month is equal to half the sum of 20% of the average of the outstanding deliverable Bonds of the four preceding Delivery Months including the current Delivery Month, and the greater of:

(A) 4,000 contracts; or

(B) 20% of the average daily Open Interest for all Delivery Months during the three calendar months preceding the Delivery Month.

Such position limits are established and published by the Bourse on a quarterly basis.

(ii) For the first Delivery Month for each designated Government of Canada Bond Futures Contract, the maximum net Long Position or net Short Position which a Person may own or control is the Futures Contract equivalent of 15% of the total outstanding amount of the cheapest-to-deliver issue of all Government of Canada Bonds eligible for Delivery for the designated Government of Canada Bond Futures Contracts ~~at market close on the fourth business day prior to the first business day of the first Delivery Month. Such position limits become effective at the market close on the first business day of the first Delivery Month~~.

Such position limits will be established and published by the Bourse in the month preceding the Delivery Month, and become effective at the market close on the first business day of the first Delivery Month.

APPENDIX B—CLEAN VERSION OF THE AMENDMENTS

Article 6.309B Position Limits for Futures Contracts

Except as otherwise indicated and except for Share Futures Contracts, the applicable position limits for Futures Contracts are as follows:

[...]

(b) Government of Canada Bond Futures:

(i) For all expiration months combined for each designated Government of Canada Bond Futures Contract, the maximum net Long Position or net Short Position which a Person may own or control at the close of trading on the first business day of the month following the Delivery Month is equal to half the sum of 20% of the average of the outstanding deliverable Bonds of the four preceding Delivery Months including the current Delivery Month, and the greater of:

(A) 4,000 contracts; or

(B) 20% of the average daily Open Interest for all Delivery Months during the three calendar months preceding the Delivery Month.

Such position limits are established and published by the Bourse on a quarterly basis.

(ii) For the first Delivery Month for each designated Government of Canada Bond Futures Contract, the maximum net Long Position or net Short Position which a Person may own or control is the Futures Contract equivalent of 15% of the total outstanding amount of the cheapest-to-deliver issue of all Government of Canada Bonds eligible for Delivery for the designated Government of Canada Bond Futures Contracts.

Such position limits will be established and published by the Bourse in the month preceding the Delivery Month, and become effective at the market close on the first business day of the first Delivery Month.