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CIRCULAR
September 28, 2007

EQUITY MARGIN PROJECT – PHASE 1 OF RULE AMENDMENT IMPLEMENTATION

AMENDMENTS TO ARTICLES 7201 TO 7204 AND ARTICLE 7213

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved amendments to articles 7201 to 7204 and article 7213 of the Rules of the Bourse regarding the margining of equity and related securities. These amendments are effective immediately.

Present rules and equity margin project – Phase 1 rule amendments

When a margin rate for a security is established, it is intended that it is sufficient to cover the risk of loss associated with the security, specifically market risk. The existing methodology for determining a listed equity security's margin rate is based on its market price per share.

Studies undertaken by the Investment Dealers Association of Canada indicated that market price per share was not an accurate indicator of a listed equity security's market risk. While determining margin rates on this basis may be operationally easy to apply, its use has resulted in margin deposits and “strategy-based” margin rules that do not reflect the true economic risk of positions in and offsets involving equity securities.

To address these issues, a new approach to determining listed equity security margin rates has been adopted. This new approach, referred to as the “basic margin rate” methodology, is essentially a methodology for determining a customized margin rate for each listed equity security. The objective of this methodology is to determine an overall margin rate for each equity security that will more accurately address its market risk. This methodology will replace the existing market price per share based rates as the standard margin rate methodology to be used by all Canadian approved participants and their customers for all Canadian and U.S. listed equity securities.

In order to implement this new methodology, the relevant rule amendments are being implemented in two phases. ***In this first phase, Phase 1, all amendments other than those that will implement the new “basic margin rate” methodology are being implemented.*** Specifically, amendments to the Rules of the Bourse are the following ones.

Article 7201, *Margin Requirements*, is amended by adding thereto a clarification to specify that the margin requirements set forth in Section 7201 – 7250 of the Rules Manual apply, unless specified otherwise, to both approved participants and their clients.

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Amendment no.: 008-2007

Article 7202, *Listed Securities*, is amended to:

1. deny margin eligibility to all listed securities whose listing requirements do not include adequate requirements regarding net earnings before taxes, net tangible assets and minimum working capital;
2. permit margin eligibility for a larger group of securities listed on foreign exchanges outside of Canada and the United States (beyond those securities listed on the first section of the Tokyo Stock Exchange First Section and on the stock list of the London Stock Exchange); and
3. make clarification changes throughout.

Article 7204 – Group V, *Corporation and trust and mortgage loan companies – non-negotiable and non-transferable debt securities*, sets out capital and margin (collectively margin) requirements for certain corporate debt instruments. Included in these requirements are rules that address the margin requirements for convertible debt instruments and convertible residual debt instruments. These requirements are amended in order to conform them with the margin requirements that would apply to an equivalent position in the underlying security and to limit the margin requirements for convertible residual debt instruments.

Article 7213, *Exceptions to Margin Rules*, is amended to conform to the margin requirements for floating preferred shares in paragraph 7 to the margin requirements that would apply to an equivalent position in the related junior security issuance.

The most significant of these amendments is the addition to article 7202 of a new paragraph 2 (*Securities listed on some other exchanges and that are components of an index*) which will grant margin eligibility to a larger group of securities listed on foreign exchanges outside of Canada and the United States. More specifically, loan value will now be extended to securities listed on foreign exchanges using a 50 percent margin rate provided:

- A) the exchange on which the security is listed is included on a list of exchanges and associations that qualify as “recognized exchanges and associations” for the purposes of determining “regulated entities”; and
- B) the security is a constituent security on the exchange’s major broadly based index.

The publication of the list mentioned in paragraph (A) above and of any updates thereto will be under the responsibility of the Investment Dealers Association of Canada (IDA). Please refer to Member Regulation Notice MR-0491 published by the IDA on September 12, 2007 for a complete list of foreign market indices whose constituent issues will now be eligible for margin at a margin rate of 50 percent. The IDA Notice also includes a list of all the constituent issues of the designated foreign indices.

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