IIROC OCRCVM
Investment Industry Regulatory Organization of Canada
Organisme canadien de réglementation du commerce des valeurs mobilières

# IIROC NOTICE

**Rules Notice**
**Request for Comments**
Dealer Member Rules

***Comments Due By: March 19, 2018***

*Please distribute internally to:*

Credit
Institutional
Internal Audit
Legal and Compliance
Operations
Regulatory Accounting
Retail
Senior Management
Trading Desk

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**18-0043**
**February 15, 2018**

## Proposed Amendments to Form 1 for use in, and consistency, with the Plain Language Dealer Member Rules Rule Book

### Executive Summary

On January 31, 2018, the Board of Directors (the **Board**) of IIROC approved the publication for comment of proposed amendments to Form 1 (the **Proposed Amendments**). The primary objective of the Proposed Amendments is to ensure that terms used in Form 1 and the Plain Language Dealer Member Rules Rule Book (the **PLR Rule Book**) are consistent.

**Impacts**

Dealer Members are expected to benefit from having defined terms that are consistent across the PLR Rule Book and Form 1.

We believe that the Proposed Amendments will have no material impact in terms of capital market structure, competition generally, cost of compliance and conformity with other rules. The Proposed Amendments do not permit unfair discrimination among customers, issuers, brokers, dealers, members or others. They do not impose any burden on competition that is not necessary or appropriate in furtherance of the above purposes. There may be minor technological implications for Dealer Members as a result of the Proposed Amendments, such as updating their systems with the new defined terms.

**How to Submit Comments**

Comments are requested on all aspects of the Proposed Amendments, including any matter which they do not specifically address. Comments on the Proposed Amendments should be in writing and delivered by **March 19, 2018** to:

Answerd Ramcharan
Manager, Financial Information, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
Suite 2000, 121 King Street West
Toronto, Ontario M5H 3T9
email: aramcharan@iiroc.ca

A copy should also be provided to the Recognizing Regulators by forwarding a copy to:

Market Regulation
Ontario Securities Commission
Suite 1903, Box 55
20 Queen Street West
Toronto, Ontario M5H 3S8
e-mail: marketregulation@osc.gov.on.ca

***Commenters should be aware that a copy of their comment letter will be made publicly available on the IIROC website at www.iiroc.ca.***

## Rules Notice - Table of Contents

## 1. Discussion of Proposed Amendments

### *1.1 Relevant background*

As detailed in Notice 17-0054 (Re-publication of Proposed IIROC Dealer Member Plain Language Rule Book), we have undertaken a project to rewrite, reformat, rationalize, and reorganize our Dealer Member Rules in plain language. The intended benefits of the PLR rewrite project are to:

(i) improve clarity and understanding of the Dealer Member Rules

(ii) focus on core requirements and move non-essential details to guidance

(iii) eliminate obsolete, duplicative and unnecessary requirements

(iv) reorganize the rule structure in a more logical way

(v) clearly state the objective of each rule.

Dealer Members are expected to benefit from having defined terms that are consistent across the PLR Rule Book and Form 1.

### *1.2 Current Form 1*

Form 1 is a special purpose report that is used by IIROC and the Canadian Investor Protection Fund (**CIPF**) to monitor the financial solvency of Dealer Members. To monitor financial solvency, IIROC monitors the risk adjusted capital level and early warning test compliance of each Dealer Member.

### *1.3 Proposed Amendments*

The terms discussed below will be in Form 1 and the PLR Rule Book. The following is a summary of the Proposed Amendments, which are shown as black-lined changes in **Appendix A**:

(1) We have added a new defined term “acceptable exchange” for purposes of non-regulated entities and a new defined term “applicable exchange” for purposes of regulated entities. The purpose of these amendments is to minimize the potential confusion with the use of the term “recognized exchange” because:

- the Canadian Securities Administrators (**CSA**) use the same defined term and it may have a different meaning from ours
- in PLR and current Dealer Member Rules “recognized exchange” could mean an exchange that is recognized by the relevant regulatory authority in the jurisdiction, or an exchange

that relates to regulated entities as defined in Form 1, depending on the PLR and Dealer Member Rule, and it may not always clear which meaning applies

- the current Universal Market Integrity Rules (**UMIR**) use a similar term ("Exchange") that has the same meaning as the CSA's defined term.

To minimize the potential confusion with the use of the term "recognized exchange" we have added new terms:

- "acceptable exchange" for purposes of non-regulated entities and replaced the term "recognized exchange" and similar references with this new term when it relates to non-regulated entities. *[Appendix A: General Notes and Definitions, and Notes and Instructions to Schedule 2]*
- "applicable exchange" for purposes of regulated entities and replaced the term "recognized exchange" with this new term when it relates to regulated entities. In addition, related to this change, the term "applicable association" will replace "recognized association" when used in relation to regulated entities. *[Appendix A: General Notes and Definitions, and Notes and Instructions to Schedules 11 and 11A]*

We also replaced references to the words "applicable exchange" with the words "relevant exchange" when reference is made to an exchange where neither the defined term "acceptable exchange" nor "applicable exchange" is intended. *[Appendix A: Notes and Instructions to Schedule 12]*

Once the Proposed Amendments are finalized, consequential amendments will be made to the PLR Rule Book to reflect these changes where appropriate.

(2) We have changed the counterparty classification defined terms, "acceptable counterparties", acceptable institutions" and "regulated entities" to their singular form to conform with the drafting convention in the PLR Rule Book. *[Appendix A: General Notes and Definitions]*

## 2. Analysis

### *2.1 Issues and alternatives considered*

Two alternatives were considered, namely: (1) to continue to use the current Form 1; and (2) to make the amendments to Form 1 to ensure that terms used in Form 1 and the PLR Rule Book are consistent.

We selected the second alternative, because it is important that terms used in Form 1 and the PLR Rule Book are consistent as together they make up IIROC's Dealer Member Rules.

### *2.2 Comparison with similar provisions*

We did not compare the Proposed Amendments with similar provisions from other jurisdictions because we do not believe it would be relevant given the unique nature of the amendments to Form 1.

## 3. Impacts of the Proposed Amendments

Dealer Members are expected to benefit from having defined terms that are consistent across the PLR Rule Book and Form 1.

We believe that the Proposed Amendments will have no material impact in terms of capital market structure, competition generally, cost of compliance and conformity with other rules. The Proposed Amendments do not permit unfair discrimination among customers, issuers, brokers, dealers, members or others. They do not impose any burden on competition that is not necessary or appropriate in furtherance of the above purposes. There may be minor technological implications for Dealer Members as a result of the Proposed Amendments, such as updating their systems with the new defined terms.

**Technological implications and implementation plan**

The Proposed Amendments may have minor impact on Dealer Members' systems, their service providers' and other stakeholders' systems, such as updating their systems with the new defined terms. After we receive approval from our recognizing regulators, we intend to implement the Proposed Amendments at the same time as the PLR Rule Book.

## 4. Policy Development Process

### *4.1 Regulatory purpose*

The Proposed Amendments are intended to:

- *establish and maintain rules that are necessary or appropriate to govern and regulate all aspects of IIROC's functions and responsibilities as a self-regulatory entity*
- *make other necessary changes of an editorial nature (such as standardization of terminology).*

In deciding to propose the Proposed Amendments, IIROC identified that there was a need to ensure that terms used in Form 1 and the PLR Rule Book are consistent.

This need was assessed as being in the public interest and not detrimental to the best interests of the capital markets. As a result, the Board has classified the Proposed Amendments as a Public Comment Rule proposal that is not contrary to the public interest.

### *4.2 Rule making process*

IIROC developed the Proposed Amendments and briefed the IIROC policy advisory committees (the Financial and Operations Advisory Section (**FOAS**) Capital Formula Subcommittee, the FOAS Operations Subcommittee, and the full FOAS) on them. They did not raise any concerns.

## 5. Appendices

Appendix A - Black-line comparison of the Proposed Amendments to current Form 1.

**Appendix A**

**INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA**

**PROPOSED AMENDMENTS TO FORM 1, FOR USE IN, AND CONSISTENCY, WITH THE PLAIN LANGUAGE DEALER MEMBER RULES RULE BOOK**

**BLACK-LINE COMPARISON OF PROPOSED AMENDMENTS TO CURRENT FORM 1**

1. Form 1 is amended as shown by the following black-line changes:

## FORM 1 - GENERAL NOTES AND DEFINITIONS

**GENERAL NOTES:**

1. Each Dealer Member must comply with the requirements in Form 1 as approved and amended from time to time by the board of directors of the Investment Industry Regulatory Organization of Canada (the Corporation).

   Form 1 is a special purpose report that includes financial statements and schedules, and is to be prepared in accordance with International Financial Reporting Standards (IFRS), except as prescribed by the Corporation.

   Each Dealer Member must complete and file all of these statements and schedules.

2. The following are Form 1 IFRS departures as prescribed by the Corporation:

| | **Prescribed IFRS departure** |
|---|---|
| Client and broker trading balances | For client and broker trading balances, the Corporation allows the netting of receivables from and payables to the same counterparty. A Dealer Member may choose to report client and broker trading balances in accordance with IFRS. |
| Preferred shares | Preferred shares issued by the Dealer Member and approved by the Corporation are classified as shareholders' capital. |
| Presentation | Statements A and E contain terms and classifications (such as allowable and non-allowable assets) that are not defined under IFRS. For Statement E, the profit (loss) for the year on discontinued operations is presented on a pre-tax basis (as opposed to after-tax).<br>In addition, specific balances may be classified or presented on Statements A, E and F in a manner that differs from IFRS requirements. The General Notes and Definitions, and the applicable Notes and Instructions to the Statements of Form 1, should be followed in those instances where departures from IFRS presentation exist.<br>Statements B, C, and D are supplementary financial information, which are not statements contemplated under IFRS. |
| Separate financial statements on a non-consolidated basis | Consolidation of subsidiaries is not permitted for regulatory reporting purposes, except for related companies that meet the definition of a "related company" in Dealer Member Rule 1 and the Corporation has approved the consolidation.<br>Because Statement E only reflects the operational results of the Dealer Member, a Dealer Member must not include the income (loss) of an investment accounted for by the equity method. |
| Statement of cash flow | A statement of cash flow is not required as part of Form 1. |
| Subordinated loan | For regulatory reporting purposes, a subordinated loan must be reported at face value. Discounting of the subordinated loan amount is not permitted. |
| Valuation | The "market value of securities" definition remains unchanged from the pre-IFRS changeover Joint Regulatory Financial Questionnaire and Report. |

3. The following are Form 1 prescribed accounting treatments based on available IFRS alternatives:

| | **Prescribed accounting treatment** |
|---|---|
| Hedge accounting | Hedge accounting is not permitted for regulatory reporting purposes. All security and derivative positions of a Dealer Member must be marked-to-market at the reporting date. Gains or losses of the hedge positions must not be deferred to a future point in time. |
| Securities owned and sold short as held-for-trading | A Dealer Member must categorize all inventory positions as held-for-trading financial instruments. These security positions must be marked-to-market. |

| | |
|---|---|
| | Because the Corporation does not permit the use of the available for sale and held-to-maturity categories, a Dealer Member must not include other comprehensive income (OCI) and will not have a corresponding reserve account relating to marking-to-market available for sale security positions. |
| Valuation of a subsidiary | A Dealer Member must value subsidiaries at cost. |

4. These statements and schedules are prepared in accordance with the Dealer Member rules.
5. For purposes of these statements and schedules, the accounts of related companies that meet the definition of a "related company" in Dealer Member Rule 1 may be consolidated.
6. For the purposes of the statements and schedules, the capital calculations must be on a trade date reporting basis unless specified otherwise in the Notes and Instructions to Form 1.
7. Dealer Members may determine margin deficiencies for clients, brokers and dealers on either a settlement date basis or trade date basis. Dealer Members may also determine margin deficiencies for *acceptable institutions*, *acceptable counterparties*, regulated entities and investment counselors' accounts as a block on either a settlement date basis or trade date basis and the remaining clients, brokers and dealer accounts on the other basis. In each case, Dealer Members must do so for all such accounts and consistently from period to period.
8. Comparative figures on all statements are only required at the audit date.
9. All statements and schedules must be expressed in Canadian dollars and must be rounded to the nearest thousand.
10. Supporting details should be provided – as required - showing breakdown of any significant amounts that have not been clearly described on the statements and schedules.
11. **Mandatory security counts.** All securities except those held in segregation or safekeeping shall be counted once a month, or monthly on a cyclical basis. Those held in segregation and safekeeping must be counted once in the year in addition to the count as at the year-end audit date.

**DEFINITIONS:**

(a) **"acceptable clearing corporation"** means any clearing agency operating a central system for clearing of securities or derivatives transactions that is subject to legislation and oversight by a central or regional government authority in the country of operation. The legislation or oversight regime must provide for or recognize the clearing agency's powers of compliance and enforcement over its members or participants. The Corporation will maintain and regularly update a list of acceptable clearing corporations.

(b) **"acceptable ~~counterparties~~counterparty"** means ~~those entities~~an entity with whom a Dealer Member may deal on a value for value basis, with mark to market imposed on outstanding transactions. The entities are as follows:

1. Canadian banks, Quebec savings banks, trust companies and loan companies licensed to do business in Canada or a province thereof. Each of the aforementioned entities must have paid up capital and surplus on the last audited balance sheet (plus such other forms of capital recognized as such in their regulatory regime as well as in this capital formula, e.g. subordinated debt) in excess of $10 million and less than or equal to $100 million to qualify, provided acceptable financial information with respect to such entities is available for inspection.
2. Credit and central credit unions and regional caisses populaires with paid up capital and surplus or net worth (excluding appraisal credits but including general reserves) on the last audited balance sheet in excess of $10 million and less than or equal to $100 million, provided acceptable financial information with respect to such entities is available for inspection.
3. Insurance companies licensed to do business in Canada or a province thereof with paid up capital and surplus or net worth on the last audited balance sheet in excess of $10 million and less than or equal to $100 million, provided acceptable financial information with respect to such companies is available for inspection.
4. Canadian provincial capital cities and all other Canadian cities and municipalities, or their equivalents, with populations of 50,000 and over.
5. Mutual funds subject to a satisfactory regulatory regime with total net assets in the fund in excess of $10 million.

6. Corporations (other than regulated entities) with a minimum net worth of $75 million on the last audited balance sheet, provided acceptable financial information with respect to such corporation is available for inspection.
7. Trusts and limited partnerships with minimum total net assets on the last audited balance sheet in excess of $100 million, provided acceptable financial information with respect to such trust or limited partnership is available for inspection.
8. Canadian pension funds which are regulated either by the Office of Superintendent of Financial Institutions or a provincial pension commission, with total net assets on the last audited balance sheet in excess of $10 million, provided that in determining net assets the liability of the fund for future pension payments shall not be deducted.
9. Foreign banks and trust companies subject to a satisfactory regulatory regime with paid up capital and surplus on the last audited balance sheet in excess of $15 million and less than or equal to $150 million, provided acceptable financial information with respect to such entities is available for inspection.
10. Foreign insurance companies subject to a satisfactory regulatory regime with paid up capital and surplus or net worth on the last audited balance sheet in excess of $15 million, provided acceptable financial information with respect to such companies is available for inspection.
11. Foreign pension funds subject to a satisfactory regulatory regime with total net assets on the last audited balance sheet in excess of $15 million, provided that in determining net assets the liability of the fund for future pension payments shall not be deducted.
12. Federal governments of foreign countries which do not qualify as a *Basel Accord country*.

For the purposes of this definition, a satisfactory regulatory regime will be one within *Basel Accord countries*.

Subsidiaries (excluding regulated entities) whose business falls in the category of any of the above enterprises and whose parent or affiliate qualifies as an acceptable counterparty may also be considered as an acceptable counterparty if the parent or affiliate provides a written unconditional irrevocable guarantee, subject to approval by the Corporation.

(c) "**acceptable exchange**" means any entity operating as an exchange for securities or derivatives transactions that is subject to legislation and oversight by a central or regional government authority in the country of operation. The legislation or oversight regime must provide for or recognize the exchange's powers of compliance and enforcement over its members or participants.

(d) **"acceptable ~~institutions~~institution"** means ~~those entities~~an entity with which a Dealer Member is permitted to deal on an unsecured basis without capital penalty. The entities are as follows:

1. Government of Canada, the Bank of Canada and provincial governments.
2. All crown corporations, instrumentalities and agencies of the Canadian federal or provincial governments which are government guaranteed as evidenced by a written unconditional irrevocable guarantee or have a call on the consolidated revenue fund of the federal or provincial governments.
3. Canadian banks, Quebec savings banks, trust companies and loan companies licensed to do business in Canada or a province thereof. Each of the aforementioned entities must have paid up capital and surplus on the last audited balance sheet (plus such other forms of capital recognized as such in their regulatory regime as well as in this capital formula, e.g. subordinated debt) in excess of $100 million, provided acceptable financial information with respect to such entities is available for inspection.
4. Credit and central credit unions and regional caisses populaires with paid up capital and surplus (excluding appraisal credits but including general reserves) on the last audited balance sheet in excess of $100 million, provided acceptable financial information with respect to such entities is available for inspection.
5. Federal governments of *Basel Accord countries*.
6. Foreign banks and trust companies subject to a satisfactory regulatory regime with paid up capital and surplus on the last audited balance sheet in excess of $150 million, provided acceptable financial information with respect to such entities is available for inspection.
7. Insurance companies licensed to do business in Canada or a province thereof with paid up capital and surplus or net worth on the last audited balance sheet in excess of $100 million, provided acceptable financial information with respect to such companies is available for inspection.
8. Canadian pension funds which are regulated either by the Office of Superintendent of Financial Institutions or a provincial

pension commission, and with total net assets on the last audited balance sheet in excess of $200 million, provided that in determining net assets the liability of the fund for future pension payments shall not be deducted.

9. Foreign pension funds subject to a satisfactory regulatory regime with total net assets on the last audited balance sheet in excess of $300 million, provided that in determining net assets the liability of the fund for future pension payments shall not be deducted.

For the purposes of this definition, a satisfactory regulatory regime will be one within *Basel Accord countries*.

Subsidiaries (other than regulated entities) whose business falls in the category of any of the above enterprises and whose parent or affiliate qualifies as an acceptable institution may also be considered as an acceptable institution if the parent or affiliate provides a written unconditional irrevocable guarantee, subject to approval by the Corporation.

(~~d~~e) **"acceptable securities locations"** means those entities considered suitable to hold securities on behalf of a Dealer Member, for both inventory and client positions, without capital penalty, given that the locations meet the requirements outlined in the segregation rules of the Corporation including, but not limited to, the requirement for a written custody agreement outlining the terms upon which such securities are deposited and including provisions that no use or disposition of the securities shall be made without the prior written consent of the Dealer Member and the securities can be delivered to the Dealer Member promptly on demand. The entities are as follows:

1. Depositories and Clearing Agencies

   Any securities depository or clearing agency operating a central system for handling securities or equivalent book-based entries or for clearing of securities or derivatives transactions that is subject to legislation and oversight by a central or regional government authority in the country of operation. The legislation or oversight regime must provide for or recognize the securities depository's or clearing agency's powers of compliance and enforcement over its members or participants. The Corporation will maintain and regularly update a list of those depositories and clearing agencies that comply with these criteria.

2. *Acceptable institutions* and subsidiaries of *acceptable institutions* that satisfy the following criteria:

   (a) *Acceptable institutions* which in their normal course of business offer custodial security services; or

   (b) Subsidiaries of *acceptable institutions* provided that each such subsidiary, together with the *acceptable institution*, has entered into a custodial agreement with the Dealer Member containing a legally enforceable indemnity by the *acceptable institution* in favour of the Dealer Member covering all losses, claims, damages, costs and liabilities in respect of securities and other property held for the Dealer Member and its clients at the subsidiary's location.

3. Acceptable counterparties - with respect to security positions maintained as a book entry of securities issued by the *acceptable counterparty* and for which the *acceptable counterparty* is unconditionally responsible.

4. Banks and trust companies otherwise classified as *acceptable counterparties* - with respect to securities for which they act as transfer agent and for which custody services are not being provided (in such case, a written custody agreement is not required).

5. Mutual Funds or their Agents - with respect to security positions maintained as a book entry of securities issued by the mutual fund and for which the mutual fund is unconditionally responsible.

6. *Regulated entities*.

7. Foreign institutions and securities dealers that satisfy the following criteria:

   (a) the paid-up capital and surplus according to its most recent audited balance sheet is in excess of Canadian $150 million as evidenced by the audited financial statements of such entity;

   (b) in respect of which a foreign custodian certificate has been completed and signed in the prescribed form by the Dealer Member's board of directors or authorized committee thereof;

   provided that:

   (c) a formal application in respect of each such foreign location is made by the Dealer Member to the Corporation in the form of a letter enclosing the financial statements and certificate described above; and

   (d) the Dealer Member reviews each such foreign location annually and files a foreign custodian certificate with the Corporation annually.

8. For London Bullion Market Association (LBMA) gold and silver good delivery bars, means those entities considered suitable to hold these bars on behalf of a Dealer Member, for both inventory and client positions, without capital penalty. These entities must:

   - be a market making member, ordinary member or associate member of the LBMA;
   - be on the Corporation's list of entities considered suitable to hold LBMA gold and silver good delivery bars; and
   - have executed a written precious metals storage agreement with the Dealer Member, outlining the terms upon which such LBMA good delivery bars are deposited. The terms must include provisions that no use or disposition of these bars shall be made without the written prior consent of the Dealer Member, and these bars can be delivered to the Dealer Member promptly on demand. The precious metals storage agreement must provide equivalent rights and protection to the Dealer Member as the standard securities custodial agreement.

and such other locations which have been approved as acceptable securities locations by the Corporation.

(~~e~~f) **"Basel Accord countries"** means those countries that are members of the Basel Accord and those countries that have adopted the banking and supervisory rules set out in the Basel Accord. [The Basel Accord, which includes the regulating authorities of major industrial countries acting under the auspices of the Bank for International Settlements (B.I.S.), has developed definitions and guidelines that have become accepted standards for capital adequacy.] A list of current Basel Accord countries is included in the most recent list of foreign *acceptable institutions* and foreign *acceptable counterparties*.

(~~f~~g) **"broad based index"** means an equity index whose underlying basket of securities is comprised of:

1. thirty or more securities;
2. the single largest security position by weighting comprises no more than 20% of the overall *market value* of the basket of equity securities;
3. the average market capitalization for each security position in the basket of equity securities underlying the index is at least $50 million;
4. the securities shall be from a broad range of industries and market sectors as determined by the Corporation to represent index diversification; and
5. 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~~an *applicable exchange*, as set out in the definition of "*regulated* ~~entities~~*entity*" in the General Notes and Definitions.

(~~g~~h) **"market value"** of a security means:

(i) For securities, precious metals bullion and commodity futures contracts quoted on an active market, the published price quotation using:

(A) For listed securities, the last bid price of a long security and, correspondingly, the last ask price of a short security, as shown on a consolidated pricing list or exchange quotation sheet as of the close of business on the relevant date or last trading date prior to the relevant date, as the case may be,

(B) For unlisted investment funds, the net asset value provided by the manager of the fund on the relevant date,

(C) For all other unlisted securities (including unlisted debt securities) and precious metals bullion, a value determined as reasonable from published market reports or inter-dealer quotation sheets on the relevant date or last trading day prior to the relevant date, or, in the case of debt securities, based on a reasonable yield rate,

(D) For commodity futures contracts, the settlement price on the relevant date or last trading day prior to the relevant date,

(E) For money market fixed date repurchases (no borrower call feature), the price determined by applying the current yield for the security to the term of maturity from the repurchase date. This will permit calculation of any profit or loss based on the market conditions at the reporting date,

(F) For money market open repurchases (no borrower call feature), the price determined as of the reporting date or the date the commitment first becomes open, whichever is the later. The value is to be determined as in (E) and the commitment price is to be determined in the same manner using the yield stated in the repurchase commitment, and

(G) For money market repurchases with borrower call features, the borrower call price and after making any adjustments considered by the Dealer Member to be necessary to accurately reflect the market value,

(ii) Where a reliable price for the security, precious metals bullion or commodity futures contract cannot be determined:

(A) The value determined by using a valuation technique that includes inputs other than published price quotations that are observable for the security, either directly or indirectly; or

(B) Where no observable market data-related inputs are available, the value determined by using unobservable inputs and assumptions; or

(C) Where insufficient recent information is available and/or there is a wide range of possible values and cost represents the best value estimate that range, cost.

(iii) Where a value cannot be reliably determined under subsections (g)(i) and (g)(ii) above, the amount used:

(A) To report the total market value of a Dealer Member securities position; and

(B) To calculate the margin requirement for a client account securities position;

shall be zero.

(~~h~~i) **"regulated ~~entities~~entity"** means ~~those entities~~an entity with whom a Dealer Member may deal on a value for value basis, with mark to market imposed on outstanding transactions. The ~~entities are~~entity is a participating ~~institutions~~institution in the Canadian Investor Protection Fund or ~~members of recognized exchanges and associations. For the purposes of this definition recognized exchanges and associations mean those entities that meet~~member of an *applicable exchange* or *applicable association*.

For regulated entity purposes an applicable exchange or applicable association means an entity that meets the following criteria:

1. the exchange or association maintains or is a member of an investor protection regime equivalent to the Canadian Investor Protection Fund;
2. the exchange or association requires the segregation by its members of customers' fully paid for securities;
3. the exchange or association rules set out specific methodologies for the segregation of, or reserve for, customer credit balances;
4. the exchange or association has established rules regarding Dealer Member and customer account margining;
5. the exchange or association is subject to the regulatory oversight of a government agency or a self-regulatory organization under a government agency which conducts regular examinations of its members and monitors member's regulatory capital on an ongoing basis; and
6. the exchange or association requires regular regulatory financial reporting by its members.

A list of current ~~recognized~~*applicable exchanges* and *applicable associations* is included in the most recent list of foreign *acceptable institutions* and foreign *acceptable counterparties*.

(~~i~~j) **"settlement date - extended"** means a transaction (other than a mutual fund security redemption) in respect of which the arranged settlement date is a date after regular settlement date.

(~~j~~k) **"settlement date - regular"** means the settlement date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs, including foreign jurisdictions. For margin purposes, if such settlement date exceeds 15 business days past trade date, settlement date will be deemed to be 15 business days past trade date. In the case of new issue trades, regular settlement date means the contracted settlement date as specified for that issue.

## FORM 1, PART II – SCHEDULE 2
## NOTES AND INSTRUCTIONS

**Valuation and margin rates**

All securities are to be valued at market (see General Notes and Definitions) as of the reporting date. The margin rates to be used are those outlined in the Corporation rules.

**All securities owned and sold short**

Schedule 2 summarizes **all** securities owned and sold short by the categories indicated. Details that must be included for each category are total long *market value*, total short *market value* and total margin required as indicated.

**Margining of option positions**

Where the Dealer Member utilizes the computerized options margining program of ~~a recognized Exchange~~an *acceptable exchange* operating in Canada, the margin requirement produced by such program may be used provided the positions in the Dealer Member's records agree with the positions in the ~~Exchange~~exchange's computer. No details of such positions are to be reported if the programs are employed. Details of any adjustments made to the margin calculated by ~~an Exchange~~the exchange's computer-margining program must be provided. For the purposes of this paragraph, ~~recognized Exchange means~~an *acceptable exchange* operating in Canada is limited to The Montreal Exchange.

**Request for detailed information**

The Examiners and/or Auditors of the Corporation may request additional details of securities owned or sold short as they, in their discretion, believe necessary.

**Margin offsets**

Where there are margin offsets between categories, the residual should be shown in the category with the larger initial margin required before offsets.

**Line 1 -** Money market is to include Canadian & US Treasury Bills, Bankers Acceptances, Bank paper (Domestic & Foreign), Municipal and Commercial Paper or other similar instruments.

**Supplementary instructions for reporting money market commitments:**

**"Market Price"** for money market commitments [fixed-term repurchases, calls, etc.] shall be calculated as follows:

(i) Fixed date repurchases [no borrower call feature] - the market price is the price determined by applying the current yield for the security to the term of maturity from the repurchase date. This will permit calculation of any profit or loss based on the market conditions at the reporting date. Exposure due to future changes in market conditions is covered by the margin rate.

(ii) Open repurchases [no borrower call feature] - prices are to be determined as of the reporting date or the date the commitment first becomes open, whichever is the later. Market price is to be determined as in (i) and commitment price is to be determined in the same manner using the yield stated in the repurchase commitment.

(iii) Repurchase with borrower call features - the market price is the borrower call price. No margin is required where the total consideration for which the holder can put the security back to the dealer is less than the total consideration for which the dealer may put the security back to the issuer. However, where a holder consideration exceeds dealer consideration [the dealer has a loss], the margin required is the lesser of:

  (a) the prescribed rate appropriate to the term of the security, and

  (b) the spread between holder consideration and dealer consideration [the loss] based on the call features subject to a minimum of 1/4 of 1% margin.

**Line 7 -** Registered traders, specialists and market makers margin requirements are:

(i) The minimum margin requirement for each TSX registered trader is $50,000.

(ii) The minimum margin requirement for each MX registered specialist is the lesser of $50,000 or an amount sufficient to assume a position of twenty board lots of each security in which such specialist is registered, subject to a maximum of $25,000 per issuer.

(iii) The market maker minimum margin requirement is for the TSX $50,000 for each specialist appointed and for the MX $10,000 for each security and/or class of options appointed (not to exceed $25,000 for each market maker in each preceding case). No minimum margin is required where the market maker does not have an appointment.

The above-noted minimum margin for each registered trader, specialist, or market maker may be applied as an offset to reduce any margin on positions held long or short in the registered trading account of such registered trader, specialist or market maker. It cannot be used to offset margin required for any other registered trader, specialist or market maker or for any other security positions of the Dealer Member.

The *market value*s related to positions in registered traders, specialists and market maker accounts should be included in the appropriate categories in the preceding lines of the Schedule. Related margin in excess of the minimum margin reported on this line should also be included in the preceding lines.

**Line 9 -** The securities to be included are Canadian bank paper with an original term of 1 year or less and bonds, debentures, treasury bills and other securities with a term of 1 year or less, of or guaranteed by the Government of Canada or a Province of Canada, the United Kingdom, the United States of America and any other national foreign government (provided such other foreign government is a member of the Basel Accord and that the securities are currently rated Aaa or AAA by Moody's Investors Service, Inc. or Standard & Poor's Corporation, respectively), which are segregated and held separate and apart from the Dealer Member's property.

**Line 12 -** Include margin reductions from offsets against IA reserves only to the extent there is a written agreement between the Dealer Member and the trader permitting the Dealer Member to recover realized or unrealized losses from the IA reserve account. Include margin reductions arising from guarantees relating to inventory accounts by Partners, Directors, and Officers of the Dealer Member (PDO Guarantees).

## FORM 1, PART II – SCHEDULES 11 AND 11A

## NOTES AND INSTRUCTIONS

1. The purpose of this Schedule is to measure the balance sheet exposure a Dealer Member has to foreign currency risk. Schedule 11A must be completed for each foreign currency that has margin requirement greater than or equal to $5,000.
2. The following is a summary of the quantitative and qualitative criteria for Currency Groups 1-4. Dealer Members should refer to the most recently published listing by SROs of currency groupings.
   - **Currency Group 1** consists of the US dollar.
   - **Currency Group 2** consists of all countries whose currencies have a historical volatility of less than 3% relative to the Canadian dollar, are quoted on a daily basis by a Canadian Schedule 1 chartered bank, and are either a member of the European Monetary System and a participant of the Exchange Rate Mechanism or there is a listed future for the currency on ~~a recognized futures~~an *applicable exchange* such as the Chicago Mercantile Exchange (CME) or Philadelphia Board of Trade (PBOT).
   - **Currency Group 3** consists of all countries whose currencies have a historical volatility of less than 10% relative to the Canadian dollar, are quoted on a daily basis by a Canadian Schedule 1 chartered bank and are a full member of the International Monetary Fund (IMF).
   - **Currency Group 4** consists of all countries, which do not satisfy the quantitative and qualitative criteria for Currency Groups 1-3.
3. Reference should be made to the applicable rules and interpretation notices of the Corporation for definitions and calculations.
4. Monetary assets and liabilities are money or claims to money, the values of which, whether denominated in foreign or domestic currency are fixed by contract or otherwise.
5. All monetary assets and liabilities as well as the Dealer Member's own foreign currency future and forward commitments are to be reported on a trade date basis.
6. Monetary liabilities and the Dealer Member's own foreign currency future and forward commitments should be disclosed by maturity dates i.e. less than or equal to two (2) years and greater than two (2) years.
7. Weighted value is calculated for foreign exchange positions with terms to maturity of greater than two (2) business days. The weighted value is derived by taking the term to maturity of the foreign exchange position in calendar days divided by 365 (weighting factor) and multiplying it by the unhedged foreign exchange amount.
8. The total margin requirement is the sum of the spot risk margin and the term risk margin requirements. The spot risk margin rates apply to all unhedged foreign exchange positions regardless of term to maturity. The term risk margin rates apply to all unhedged foreign exchange positions with a term to maturity of greater than two (2) business days. The following summarizes the margin rates by Currency Group:

| | **Currency Group** | | | |
|---|---|---|---|---|
| | **1** | **2** | **3** | **4** |
| Spot Risk Margin Rate (Note 1) | 1.0% | 3.0% | 10% | 25% |
| Term Risk Margin Rate (Note 2) | 1.0% to a maximum of 4% | 3.0% to a maximum of 7% | 5.0% to a maximum of 10% | 12.5% to a maximum of 25% |
| Total Maximum Margin Rates (Note 1) | 5% | 10% | 20% | 50% |

**Note 1**: Spot risk margin rates may be subject to the Foreign Exchange Margin Surcharge

**Note 2**: If the weighting factor described in 7 above exceeds the maximum term risk margin rate in the above table, the weighting factor should be adjusted to the maximum.

9. Dealer Members may elect to exclude non-allowable monetary assets from the total monetary assets reported on Schedule 11A for purposes of the foreign exchange margin calculation. The reason underlying this proviso is that a Dealer Member should not have to provide foreign exchange margin on a non-allowable asset which is already fully provided for in the determination of the capital position of the Dealer Member unless it serves as an economic hedge against a monetary liability.
10. For Dealer Members offsetting an inventory futures contract/forward contract position in which there is a futures contract for the currency listed on ~~a recognized~~an *applicable exchange*, an alternative margin calculation may be used (refer to rules and interpretation notices of the Corporation). Any contract positions for which the margin is calculated under the alternative method must be reported as part of the inventory margin calculations on Schedule 2 and should be excluded from Schedule 11A.
11. Line 20 - The Foreign Exchange Concentration Charge applies only to currencies in Groups 2 to 4.

## FORM 1, PART II – SCHEDULE 12
## NOTES AND INSTRUCTIONS

1. The purpose of Schedule 12 is to ensure that there is adequate capital available at a Dealer Member to cover concentration risks regarding positions in futures contracts and short futures contract options and counterparty risk related to deposits with correspondent brokers.

2. For the purposes of this schedule the term:

   (i) **"correspondent broker"** means a broker who is registered to engage in soliciting or accepting and handling orders for the purchase or sale of futures contracts or futures contract options on the behalf of the Dealer Member in a country other than Canada;

   (ii) **"futures contracts"** includes commodity futures and financial futures contracts;

   (iii) **"long futures contract positions"** includes futures contracts underlying short put options on futures contracts;

   (iv) **"maintenance margin requirements"** means the requirements prescribed by the futures exchange on which the futures contracts were entered into; and

   (v) **"short futures contract positions"** includes futures contracts underlying short call options on futures contracts.

3. **Line 1 - General margin provision (Notes 3 and 4)**

   Line 1 is used to establish a base level of capital that a Dealer Member is to provide when the maintenance margin requirements (calculated and published by the futures exchange in which the futures contracts and futures contract options are entered) are not calculated on a daily basis. The base level of capital is dependent on the number and type of contracts currently held by the Dealer Member and its clients.

   The general margin provision calculation is on the Dealer Member and client account open positions in futures contracts and futures contract options, except for the specified excluded positions in the related Note below.

   The margin required is 15% of the greater of:

   (i) the maintenance margin requirements of the total long futures contract positions for each type of futures contract carried for all Dealer Member and client accounts; or

   (ii) the maintenance margin requirements of the total short futures contract positions for each type of futures contract carried for all Dealer Member and client accounts.

   Where a futures exchange calculates and publishes maintenance margin requirements on a daily basis, no margin is required under Line 1.

4. **Excluded positions from the calculation of Line 1**

   (i) Positions held in accounts of acceptable institutions, acceptable counterparties and regulated entities.

   (ii) Hedge positions (as opposed to speculative positions) where the underlying interest is held in the client's account at the Dealer Member or that the Dealer Member has a document giving the Dealer Member an irrevocable right to take possession of the underlying interest and deliver it at the location designated by the appropriate clearing corporation.

   All other hedge positions are treated as speculative positions for the purpose of this calculation.

   (iii) Dealer Member or individual client spread positions in futures contracts in the same product (including futures contracts in the same product with different delivery months) entered into on the same futures exchange.

   All other spread positions are treated as speculative positions for the purpose of this calculation.

   (iv) Dealer Member or individual client short option positions on futures contracts which are out-of-the-money by more than two maintenance margin requirements.

   (v) Dealer Member or individual client spread positions in the same futures contract options.

**FORM 1, PART II – SCHEDULE 12**

**NOTES AND INSTRUCTIONS** [Continued]

5. **Line 2 - Concentration in individual accounts (Notes 5, 6 and 9)**

Line 2 requires capital to be provided to cover concentration risk in individual accounts (client or the Dealer Member) when the aggregate of the maintenance margin requirements for each type of futures contract position or underlying interest on futures contract option position held both long and short for individual clients (including groups of clients or related clients) or in the Dealer Member's inventory is greater than 15% of the Dealer Member's net allowable assets. The concentration risk is the excess amount of the aggregate of those maintenance margin requirements over 15% of the Dealer Member's net allowable assets.

The capital to be provided is dependent on the excess amount calculation below (which allows for specified deductions and excluded positions in the related Notes below) and how quickly the Dealer Member eliminates this concentration risk.

Spread positions in the same product or different product on the same exchange and an inter-exchange or inter-commodity spread could be included using the maintenance margin as set by the exchange, provided that the spread is acceptable for margin purposes by the ~~applicable~~relevant exchange.

The excess amount is:

(i) the aggregate of the maintenance margin requirements for each type of futures contract position or underlying interest on futures contract option position held both long and short for individual clients (including groups of clients or related clients) or in the Dealer Member's inventory, except for positions mentioned in Note 9; minus

(ii) 15% of the Dealer Member's net allowable assets.

Margin is required on the close of the third trading day after the concentration first occurred and is the lesser of:

(i) the excess amount calculated when the concentration first occurred; and

(ii) the excess amount, if any, that exists on the close of the third trading day.

6. **Deductions from Part (i) of the excess amount calculation of Line 2**

(i) Any excess margin in the Dealer Member account or client's account is to be deducted from Part (i) of the excess amount calculation. The excess margin is to be based on the maintenance margin.

7. **Line 3 - Concentration in individual open futures contracts and short options on futures contract positions (Notes 7 to 9)**

Line 3 requires capital to be provided to cover concentration risk in individual open futures contracts and short options on futures contract positions when the aggregate of two maintenance margin requirements on the greater of the long or the short futures contracts positions for each type of futures contract position or underlying interest of futures contract option position, held in both the Dealer Member's inventory and for all clients, is greater than 40% of the Dealer Member's net allowable assets. The concentration risk is the excess amount of those aggregate of two maintenance margin requirements over 40% of the Dealer Member's net allowable assets.

The capital to be provided is dependent on the excess amount calculation below (which allows for specified deductions and excluded positions in the related Notes below) and how quickly the Dealer Member eliminates this concentration risk.

Spread positions in the same product or different product on the same exchange and an inter-exchange or inter-commodity spread could be included using the maintenance margin as set by the exchange, provided that the spread is acceptable for margin purposes by the ~~applicable~~relevant exchange.

The excess amount is:

(i) the aggregate of two maintenance margin requirements on the greater of the long or the short futures contracts positions for each type of futures contract position or underlying interest of futures contract option position, held in both the Dealer Member's inventory and for all clients, except for positions mentioned in Note 9; minus

(ii) 40% of the Dealer Member's net allowable assets.

Margin is required on the close of the third trading day after the concentration first occurred and is the lesser of:

(i) the excess amount calculated when the concentration first occurred; and

**FORM 1, PART II – SCHEDULE 12**

**NOTES AND INSTRUCTIONS** [Continued]

(ii) the excess amount, if any, that exists on the close of the third trading day.

8. **Deductions from Part (i) of the excess amount calculation of Line 3**

(i) Any excess margin may be deducted from Part (i) of the excess amount calculation, up to two maintenance margin requirements in the Dealer Member account or client's account (on a per client basis). The excess margin is to be based on the maintenance margin.

9. **Excluded positions from Part (i) of the excess amount calculation of Lines 2 and 3**

(i) Positions held in accounts of acceptable institutions, acceptable counterparties and regulated entities.

(ii) Hedge positions (as opposed to speculative positions), where the underlying interest is held in the client's account at the Dealer Member or that the Dealer Member has a document giving the Dealer Member an irrevocable right to take possession of the underlying interest and deliver it at the location designated by the appropriate clearing corporation.

All other hedge positions are treated as speculative positions and are thereby not excluded.

(iii) The following short option positions on futures contracts in a Dealer Member or client account, and provided that the pairings are acceptable for margin purposes by the ~~applicable~~relevant exchange:

(a) short calls or puts which are out-of-the-money by more than two maintenance margin requirements;

(b) a short call and a short put pairing on the same futures contract with the same exercise price and same expiration month;

(c) a futures contract paired with an in-the-money option;

(d) a short call (put) paired with a long in-the-money call (put);

(e) a short call (put) paired with a long (short) futures contract;

(f) an out-of-the-money short call paired with an out-of-the-money long call, where the strike price of the short call exceeds the strike price of the long call; and

(g) an out-of-the-money short put paired with an out-of-the-money long put.

10. **Line 4 - Margin on deposits with correspondent brokers**

(i) Where a correspondent broker owes assets (including cash, open trade equity and securities) to a Dealer Member exceeding 50% of the Dealer Member's net allowable assets, the excess amount must be provided as a charge in computing the Dealer Member's margin required.

The assets owing to the Dealer Member are the amount of deposits before reducing this amount by the maintenance margin requirements for all open positions.

(ii) Where the net worth of the correspondent broker (as determined from its latest published audited financial statements) is:

(a) greater than $50,000,000, no margin is required under this rule;

(b) less than or equal to $50,000,000, the Dealer Member must provide the amount calculated in Note 10(i).

(iii) Where a Dealer Member who operates its futures contracts and futures contract options business on a fully disclosed basis with a correspondent broker, no exemption from this requirement is permitted.