DERIVATIVES REGULATION

Derivatives Act
(2008, c. 24, s. 175, subpars. (2) to (4), (9) to (12),(18), (26) and (29))

DIVISION I
MINIMUM ASSETS OF AN ACCREDITED COUNTERPARTY

1. The minimum assets, for the purposes of subparagraph b of paragraph 7 of the definition of accredited counterparty in section 3 of the Derivatives Act (2008, c. 24), must consist of cash, securities, insurance contracts or deposits having an aggregate realizable value, before taxes, but after deduction of the corresponding liabilities, of more than $10,000,000 or an equivalent amount in another currency.

In the case of an individual, the minimum assets held by him personally or through other persons under his control must, in the manner set forth in the first paragraph of this section, have a value of more than $5,000,000 or an equivalent amount in another currency.

DIVISION II
SELF-CERTIFICATION OF AN OPERATING RULE OF A RECOGNIZED REGULATED ENTITY

2. A recognized regulated entity that seeks selfcertification of an operating rule pursuant to section 22 of the Act must proceed in accordance with this division.

3. Subject to section 7 hereof, the entity must submit for public consultation of not less than 30 days any amendment to its operating rules governing in particular its organization, operation, market, derivatives clearing, market regulation services, any change in accessing its services or the activities of its members or participants.

To this end, it must send the proposed rule amendment to every member and participant and to the Authority, which will publish it in its Bulletin.

4. A proposed rule amendment must be accompanied by a notice of publication indicating in particular the time period during which interested parties may send comments to the persons

designated therein by the entity and the Authority.

5. The rule approved by the entity becomes enforceable when a notice self-certifying the rule is sent to the Authority by the entity at the completion of the public consultation process, if any.

6. The notice of self-certification of a rule must include the following information:

(1) the approved text;

(2) a summary of all comments made in the course of the consultation process;

(3) a summary of any research, studies or comparative evaluations carried out with respect to the measures proposed in the rule;

(4) an analysis of the advantages and disadvantages of the measures proposed in the rule as well as the reasons for which the entity believes they should be approved;

(5) the effective date of the rule;

(6) the compliance notice provided for in the first paragraph of section 22 of the Act; and

(7) any other information required from the entity, in particular pursuant to a procedure, agreement, authorization or decision.

7. The entity is not required to hold a public consultation or furnish the information stipulated in paragraphs 2 to 4 of section 6 hereof where the proposed rule meets any of the following conditions:

(1) its impact on an entity, a member or a participant thereof or on a market participant is minor;

(2) it pertains to an issue related to a routine operational process or an administrative practice;

(3) it is intended for purposes of harmonization or compliance with an existing rule or with legislation; or

(4) it corrects an error of form, a clerical error or a mistake in calculation or makes stylistic changes, such as an amendment to a title or to paragraph numbering.

The rule may pertain to a derivative already approved by the entity in accordance with section

10 hereof.

8. Where section 7 hereof applies, the entity must give the Authority the reasons thereof.

Where the Authority disagrees with the reasons, it must give the entity an explanation thereof in writing within 21 days following receipt of the rule.

The entity must then submit the rule for public consultation as provided for in this Regulation.

9. A rule may also be approved without a public consultation where the entity is of the opinion that an emergency situation so requires.

Such a rule may only become effective after a written notice has been filed with the Authority informing it of the approved text.

No later than the business day following the effective date of the rule, the reasons for the emergency must be given to the Authority together with the notice of selfcertification provided for in this Regulation, with the necessary modifications regarding the information to be included.

10. Where an entity approves a rule in respect of a new derivative, it must, no later than the effective date of the rule, send the approved text to the Authority together with information on the product, namely:

(1) a description of all the terms related to the new product, of any ancillary agreement made in respect thereof and, if applicable, of the circumstances surrounding the offer or trading thereof; and

(2) the other information required in the notice of self-certification provided for in this Regulation, with the necessary modifications.

Such a rule is not subject to public consultation.

11. A rule in respect of a derivative, whether new or already approved by the entity, sets out an attribute of a derivative or its underlying interest, or sets out a specific condition for the trading or clearing of a derivative.

DIVISION II.1
DEALERS AND ADVISERS

11.1. Regulation 31-102 respecting National Registration Database, approved by Ministerial Order

No. 2007-04
dated June 21, 2007, sections 1.1, 1.3, 2.2, 3.1 to 3.4, 3.11 to 3.13, 3.15(1), 3.16(1), 4.1, 4.2, 8.23 to 8.25, 8.30, 9.1, 9.3(1), Part 11, sections 12.1 to 12.4, 12.6 to 12.13, Part 13 and sections 14.2 to 14.14 of Regulation 31-103 respecting Registration Requirements and Exemptions, approved by Ministerial Order no. 2009-04 dated September 9, 2009, and Regulation 33-109 respecting Registration Information, approved by Ministerial Order no. 2009-05 dated September 9, 2009, apply, with the necessary modifications, to the persons contemplated in subdivision 1.

§1. Registration

11.2. A dealer must register in the category of derivatives dealer.

11.3. A dealer must participate in a contingency fund deemed acceptable by the Authority.

11.4. An adviser must register in the category of derivatives portfolio manager.

11.5. A representative must register in one of the following categories:

(1) derivatives dealing representative;

(2) derivatives advising representative;

(3) derivatives associate advising representative.

11.6. In addition to the education and experience requirements of sections 3.11 and 3.12 of Regulation 31-103 respecting Registration Requirements and Exemptions, the advising representative or the associate advising representative must meet the following requirements to act on behalf of a derivatives portfolio manager:

(1) have at least 2 years of relevant derivatives experience;

(2) have passed all required exams of the Investment Industry Regulatory Organization of Canada with respect to derivatives for a dealing representative.

11.7. To register as an ultimate designated person, a person must be designated by the derivatives dealer or portfolio manager. The dealer or portfolio manager must designate one of the following:

(1) the chief executive officer or sole proprietor of the dealer or portfolio manager;

(2) the officer in charge of a division of the dealer or portfolio manager, if the activity that

requires the dealer or portfolio manager to register occurs only within the division;

(3) an individual acting in a capacity similar to that of an officer described in paragraph (1) or (2).

11.8. The ultimate designated person must do all of the following:

(1) supervise the activities of the derivatives dealer or portfolio manager that are directed towards ensuring compliance with the Act by such dealer or portfolio manager and each officer, representative and employee of such dealer or portfolio manager;

(2) promote compliance with the Act by the derivatives dealer or portfolio manager as well as by the officers, representatives and employees of such dealer or portfolio manager.

11.9. The derivatives dealer or portfolio manager must designate a replacement for the ultimate designated person where such person no longer qualifies under section 11.7.

11.10. To register as a chief compliance officer, a person must be designated by the derivatives dealer or portfolio manager. The dealer or portfolio manager must designate one of the following:

(1) an officer or partner of the dealer or portfolio manager;

(2) the sole proprietor of the dealer or portfolio manager.

11.11. The chief compliance officer must do all of the following:

(1) establish and maintain policies and procedures for assessing compliance with the Act by the dealer or portfolio manager, and by the officers, representatives and employees of such dealer or portfolio manager;

(2) monitor and assess compliance with the Act by the dealer or portfolio manager, and by the officers, representatives and employees of such dealer or portfolio manager;

(3) report to the ultimate designated person as soon as possible if the chief compliance officer becomes aware of any circumstances indicating that the dealer, portfolio manager or any individual acting on its behalf may be in non-compliance with the Act and any of the following apply:

(a) the non-compliance creates, in the opinion of a reasonable person, a risk of harm to a client or the capital markets;

(b) the non-compliance is part of a pattern of noncompliance;

(4) submit an annual report to the dealer's or portfolio manager's board of directors, or individuals acting in a similar capacity on its behalf, for the purpose of assessing compliance with the Act by the dealer or portfolio manager, and by the officers, representatives and employees of such dealer or portfolio manager.

11.12. The derivatives dealer or portfolio manager must designate a replacement for the chief compliance officer where such officer no longer qualifies under section 11.10.

11.13. In addition to the education and experience requirements of section 3.13 of Regulation 31-103 respecting Registration Requirements and Exemptions, the chief compliance officer of a derivatives portfolio manager must meet the following requirements:

(1) have at least 3 years of relevant derivatives experience;

(2) have passed all required exams of the Investment Industry Regulatory Organization of Canada with respect to derivatives for an officer of a dealer.

§2. Exemptions

11.14. The provisions under Title III of the Act, other than section 60, do not apply to a person authorized to act as a dealer or adviser or authorized to exercise similar functions under legislation applicable in a jurisdiction outside Québec where its head office or principal place of business is located to the extent it carries on business solely for an accredited counterparty and its activity involves a standardized derivative that is offered primarily outside Québec.

11.15. The best execution obligation under the second paragraph of section 68 of the Act does not apply to an alternative trading system, where it carries out an activity of a published market and its processing of client orders is limited to accepting such orders for execution in the system.

§3. Suspension and revocation

11.16. If a registered derivatives dealer or portfolio manager has not paid the annual fees due under section 5 of the Tariffs for Costs and Fees Payable in respect of Derivatives, enacted by Order-in-Council No. 93-2009 dated February 11, 2009, by the 30th day after the date the fees were due, the registration of the dealer or portfolio manager is suspended until reinstated or revoked under the Act and this Regulation.

The first paragraph applies as well to a derivatives dealer or portfolio manager deemed to be registered under section 57 of the Act that has not paid the annual fees due under section 271.5 of the Securities Regulation, enacted by Order-in-Council No. 660-83 dated March 30, 1983.

11.17. The suspension of the registration of a dealer, adviser or any of its representatives registered under sections 148 or 149 of the Securities Act (R.S.Q., c. V-1.1) results in the suspension of the registration of a derivatives dealer or portfolio manager or its representative, as the case may be, deemed to be registered under section 57 of the Derivatives Act.

11.18. If the Investment Industry Regulatory Organization of Canada revokes or suspends the membership of a registered derivatives dealer or the authorization of a registered representative, ultimate designated person or chief compliance officer, such registration is suspended until reinstated or revoked under the Act and this Regulation.

11.19. If the registration of a derivatives dealer or portfolio manager is suspended, the registration of each registered representative acting on behalf of such dealer or portfolio manager is suspended until reinstated or revoked under the Act and this Regulation.

11.20. The registration of a representative, ultimate designated person or chief compliance officer who ceases to have authority to act on behalf of a registered derivatives dealer or portfolio manager because of the end of, or a change in, his employment, partnership, or mandatary relationship with the dealer or portfolio manager is suspended until reinstated or revoked under the Act and this Regulation.

11.21. If a registration has been suspended under this section and it has not been reinstated, the registration is revoked on the second anniversary of the suspension.

The first paragraph does not apply where a suspended registrant is party to a proceeding commenced under the Act or under the rules of an SRO.

DIVISION II.2
CLIENT BROKERAGE COMMISSIONS

11.22 Regulation 23-102 respecting Use of Client Brokerage Commissions, approves by Ministerial Order No. 2010-02 dated January 31, 2010 (2010, *G.O.* 2, 582), applies, with the necessary modifications, to dealers and advisers governed by the Act.

DIVISION III

COMMUNICATIONS WITH CLIENTS

12. The risk information document provided for in section 70 of the Act must be provided to the client by the dealer, including the text of Schedule A.

13. A dealer who gives a risk information document to a client must obtain an acknowledgement of receipt with a reference to the date of receipt.

14. The relationship disclosure document must also contain all information that the registered firm is required to obtain or confirm in accordance with section 65 of the Act.

15. This Regulation comes into force on the day section 22 of the Act comes into force.

SCHEDULE A
(Section 12)

RISK INFORMATION DOCUMENT

Risk Information Document for Derivatives

This brief document does not disclose all of the risks and other significant aspects of trading in futures contracts, options or other derivatives. In light of the risks, you should undertake such transactions only if you understand the nature of the contracts (and contractual relationships) into which you are entering and the extent of your exposure to risk. Trading in derivatives is not suitable for many members of the public. You should carefully consider whether trading is appropriate for you in light of your experience, objectives, financial resources and other relevant circumstances.

Futures Contracts

1. Effect of “Leverage” or “Gearing”

Transactions in futures contracts carry a high degree of risk. The amount of initial margin is small relative to the value of the futures contract so that transactions are “leveraged” or “geared”. A relatively small market movement will have a proportionately larger impact on the funds you have deposited or will have to deposit: this may work against you as well as for you. You may sustain a total loss of initial margin funds and any additional funds deposited with the firm to maintain your position. If the market moves against your position or margin levels are increased, you may be

called upon to pay substantial additional funds on short notice to maintain your position. If you fail to comply with a request for additional funds within the time prescribed, your position may be liquidated at a loss and you will be liable for any resulting deficit.

2. Risk-reducing Orders or Strategies

The placing of certain orders (e.g. “stop-loss” order, where permitted under local law, or “stop-limit” orders) which are intended to limit losses to certain amounts may not be effective because market conditions may make it impossible to execute such orders. Strategies using combinations of positions, such as “spread” and “straddle” positions may be as risky as taking simple “long” or “short” positions.

Options

3. Variable Degree of Risk

Transactions in options carry a high degree of risk. Purchasers and sellers of options should familiarize themselves with the type of option (i.e. put or call) which they contemplate trading and the associated risks. You should calculate the extent to which the value of the options must increase for your position to become profitable, taking into account the premium and all transaction costs.

The purchaser of options may offset or exercise the options or allow the options to expire. The exercise of an option results either in a cash settlement or in the purchaser acquiring or delivering the underlying interest. If the option is on a futures contract, the purchaser will acquire a futures position with associated liabilities for margin (see the section on Futures Contracts above). If the purchased options expire worthless, you will suffer a total loss of your investment which will consist of the option premium plus transaction costs. If you are contemplating purchasing deep-out-of-the-money options, you should be aware that the chance of such options becoming profitable ordinarily is remote.

Selling (“writing” or “granting”) an option generally entails considerably greater risk than purchasing options. Although the premium received by the seller is fixed, the seller may sustain a loss well in excess of that amount. The seller will be liable for additional margin to maintain the position if the market moves unfavourably. The seller will also be exposed to the risk of the purchaser exercising the option and the seller will be obligated to either settle the option in cash or to acquire or deliver the underlying interest. If the option is on a futures contract, the seller will acquire a position in a future with associated liabilities for margin (see the section on Futures Contracts above). If the option is “covered” by the seller holding a corresponding position in the underlying interest or a futures contract or another option, the risk may be reduced. If the option is not covered, the risk of loss can be unlimited.

Certain exchanges in some jurisdictions permit deferred payment of the option premium, exposing the purchaser to liability for margin payments not exceeding the amount of the premium. The purchaser is still subject to the risk of losing the premium and transaction costs. When the option is exercised or expires, the purchaser is responsible for any unpaid premium outstanding at that time.

Additional Risks Common to Derivatives

4. Terms and Conditions of Contracts

You should ask the firm with which you deal about the terms and conditions of the specific futures contracts, options or other derivatives which you are trading and associated obligations (e.g. the circumstances under which you may become obligated to make or take delivery of the underlying interest and, in respect of options, expiration dates and restrictions on the time for exercise).

Under certain circumstances the specifications of outstanding contracts (including the exercise price of an option) may be modified by the exchange or clearing house to reflect changes in the underlying interest.

5. Suspension or Restriction of Trading and Pricing Relationships

Market conditions (e.g. liquidity) and/or the operation of the rules of certain markets (e.g. the suspension of trading in any contract or contract month because of price limits or "circuit breakers") may increase the risk of loss by making it difficult or impossible to effect transactions or liquidate/offset positions. If you have sold options, this may increase the risk of loss.

Further, normal pricing relationships between the underlying interest and the derivative may not exist. This can occur when, for example, the futures contract underlying the option is subject to price limits while the option is not.

The absence of an underlying reference price may make it difficult to judge "fair" value.

6. Deposited Cash and Property

You should familiarize yourself with the protections accorded money or other property you deposit for domestic and foreign transactions, particularly in the event of a firm insolvency or bankruptcy. The extent to which you may recover your money or property may be governed by specific legislation or local rules. In some jurisdictions, property which had been specifically identifiable as your own will be prorated in the same manner as cash for purposes of distribution in

the event of a shortfall.

7. Commission and Other Charges

Before you begin to trade, you should obtain a clear explanation of all commissions, fees and other charges for which you will be liable. These charges will affect your net profit (if any) or increase your loss.

8. Transactions in Other Jurisdictions

Transactions on markets in other jurisdictions, including markets formally linked to a domestic market, may expose you to additional risk. Such markets may be subject to regulation which may offer different or diminished investor protection. Before you trade you should inquire about any rules relevant to your particular transactions. Your local regulatory authority will be unable to compel the enforcement of the rules of regulatory authorities or markets in other jurisdictions where your transactions have been effected. You should ask the firm with which you deal for details about the types of redress available in both your home jurisdiction and other relevant jurisdictions before you start to trade.

9. Currency Risks

The profit or loss in transactions in foreign currency-denominated derivatives (whether they are traded in your own or another jurisdiction) will be affected by fluctuations in currency rates where there is a need to convert from the currency denomination of the derivative to another currency.

10. Trading Facilities

Most open-outcry and electronic trading facilities are supported by computer-based component systems for the order-routing, execution, matching, registration or clearing of trades. As with all facilities and systems, they are vulnerable to temporary disruption or failure. Your ability to recover certain losses may be subject to limits on liability imposed by the system provider, the market, the clearing house and/or member firms. Such limits may vary; you should ask the firm with which you deal for details in this respect.

11. Electronic Trading

Trading on an electronic trading system may differ not only from trading in an open-outcry market but also from trading on other electronic trading systems. If you undertake transactions on an electronic trading system, you will be exposed to risks associated with the system, including the failure of hardware and software. The result of any system failure may be that your order is either

not executed according to your instructions or is not executed at all. Your ability to recover certain losses which are particularly attributable to trading on a market using an electronic trading system may be limited to less than the amount of your total loss.

12. Off-exchange Transactions

In some jurisdictions, and only then in restricted circumstances, firms are permitted to effect off-exchange transactions. The firm with which you deal may be acting as your counterparty to the transaction. It may be difficult or impossible to liquidate an existing position, to assess the value, to determine a fair price or to assess the exposure to risk. For these reasons, these transactions may involve increased risks.

Off-exchange transactions may be less regulated or subject to a separate regulatory regime. Before you
undertake such transactions, you should familiarize yourself with applicable rules.

Decision 2008-PDG-0272 -- December 12, 2008
Bulletin de l'Autorité : 2009-01-23, Vol. 6 n° 3
M.O. 2009-01, January 15, 2009, G.O. January 21, 2009

Amendments

Decision 2009-PDG-0125 -- September 4, 2009
Bulletin de l'Autorité : 2009-09-25, Vol. 6 n° 38
M.O. 2009-07, September 9, 2009, G.O. September 25, 2009
(Section amended : 11.1 à 11.21 (addition))

Decision 2010-PDG-0087 -- May 10, 2010
Bulletin de l'Autorité : 2010-06-18, Vol. 7 n° 24
M.O. 2010-10, June 1, 2010, G.O. June 16, 2010
(Section amended : 11.22 (addition))