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Organisme canadien de réglementation du commerce des valeurs mobilières

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15-0053
February 26, 2015

Margin requirements for certain cash and security borrowing and lending arrangements - Proposed Amendments to Schedules 1, 7 and 7A of Dealer Member Form 1

Summary of nature and purpose of proposed Rule

On January 28, 2015, the Board of Directors (the Board) of the Investment Industry Regulatory Organization of Canada (IIROC) approved the republication for comment of the proposed amendments to Schedule 1, 7 and 7A of Dealer Member Form 1 (collectively, "the Proposed Amendments"). The Proposed Amendments provide that:

- qualifying principal cash and security borrowing and lending agreements, between a Dealer Member and an "acceptable counterparty" and a "regulated entity", are subject to margin requirements that reflect the risk of loss associated with such arrangements and are comparable; and

- qualifying agency security borrowing and lending agreements are subject to the margin requirements that reflect the risk of loss associated with such arrangements.

Issues and specific proposed amendments

Relevant history

The original proposal ("Original Proposal") was published for a 90-day comment period in IIROC Notice 14-0066 on March 13, 2014. We received five public comment letters and comments from staff of the Canadian Securities Administrators ("CSA Staff"). The Original Proposal proposed:

(i) for qualifying cash and security borrowing and lending arrangements

 (a) for arrangements involving lower credit risk counterparties[1], allowing a Dealer Member to deliver a modest amount of excess collateral to the arrangement counterparty (or their agent) without having to provide margin;

 (b) making the margin requirements, where the arrangement counterparty is a "regulated entity", the same as where the arrangement counterparty is an "acceptable counterparty";

(ii) for certain agency security borrowing and lending arrangements, allowing a Dealer Member to treat the arrangement, for margin purposes, as if it was an equivalent principal arrangement executed between the Dealer Member and the custodian.

 Specifically, certain three-party agency arrangements, where the parties are the Dealer Member, a client counterparty and the counterparty's custodian acting as agent, have added risk protection features that result in no greater risk of loss than if the Dealer Member had entered into a principal arrangement with the counterparty's custodian. IIROC has determined that arrangements that qualify for this "equivalent to principal" concept are agency security borrowing and lending arrangements where:

 (a) the agent custodian is an acceptable institution; and

 (b) the agent custodian's client, the underlying principal counterparty in the agency arrangement, must be an acceptable institution, acceptable counterparty or a regulated entity;

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[1] Counterparties that qualify as an "acceptable institution", "acceptable counterparty" or "regulated entity" are considered to be a lower credit risk counterparty under IIROC Dealer Member Rules.

(iii) for resale and repurchase arrangements, requiring a Dealer Member to provide margin where it has delivered any excess amount of collateral to the counterparty that is an acceptable counterparty or a regulated entity, because overcollateralization is not a common market practice for these arrangements and overcollateralization for these arrangements would run counter to another Canadian regulator's proposal to introduce "haircuts" for these arrangements; and

(iv) for Schedule 7A (Acceptable Counterparties Financing Activities Concentration Charge), to extend the existing overcollateralization test, which currently only applies to overcollateralization exposures to acceptable counterparties, to apply overcollateralization exposures to both acceptable counterparties and regulated entities, because of the modest amount of overcollateralization that is being allowed as described in (i) above.

In response to the comments received, IIROC Staff have made material and non-material revisions to the Original Proposal (as set out in the Proposed Amendments) that

(i) broaden the scenarios in which the "equivalent to principal" concept can be applied to agency security borrowing and lending arrangements (i.e. apply the assessment of risk consistently to additional qualifying agency security borrowing and lending agreements, where the additional risk protection features are met);

(ii) further clarify the intent and scope of the amendments and margin requirements; and

(iii) make certain housekeeping amendments.

A copy of IIROC Staffs' response to the public comments received is included as Attachment D.

Key issue

A key issue addressed in the Proposed Amendments concerns certain agency security borrowing and lending arrangements. In general, security borrowing/lending transactions expose Dealer Members to potential loss despite the fact that they are collateralized transactions. The exposure results from the fact that (i) borrowings of securities by Dealer Members are typically modestly over-collateralized, (ii) both the borrowed security and collateral values may fluctuate over time giving rise to further mismatches in coverage, and (iii) in the event of the insolvency of the Dealer Member's counterparty, it may be difficult and time consuming to recover the collateral and close out the transaction – while market values continue to fluctuate.

Tri-party agency arrangements have risk protection features that mitigate a Dealer Member's risk of loss through the use of a third party custodian which stands between the borrower and lender and holds, as agent, the collateral supporting the loan on the lender's behalf. These risk protection features are:

(1) the collateral is held by the third party custodian agent, who qualifies as a "financial intermediary" under the Eligible Financial Contract Rules (*Bankruptcy and Insolvency Act*), and will not be released to the underlying principal customer. In the event of a default by the Dealer Member, the custodian would liquidate the collateral, purchase the loaned securities in the market with the proceeds and return remaining proceeds, if any, to the Dealer Member; and

(2) the agency arrangement qualifies as an "eligible financial contract" under the Eligible Financial Contract Rules (*Bankruptcy and Insolvency Act*) and therefore, in the event of an insolvency of either the custodian agent or the underlying principal customer, the collateral does not form part of the insolvent party's estate and can be quickly returned to the Dealer Member.

As a result, these agency arrangements are considered by IIROC Staff to be at most no more risky than a bi-lateral security borrowing and lending agreement between the Dealer Member and the third party custodian, as if it was acting as principal.

Consequently, under the proposed amendments, these agency arrangements would be treated, for margin purposes, in the same way as the equivalent principal arrangement would have been between the Dealer Member and the custodian, and therefore margined according to the counterparty credit risk classification of the custodian.

Typically, custodians that are active in the security borrowing and lending business are financial institutions (e.g. CIBC Mellon, BNY Mellon, State Street) that meet the definition of "acceptable institutions" and are considered the lowest credit risk clients under IIROC's counterparty credit risk classification.

Reason for republication

The revisions to the Original Proposal would:

(i) consistently apply the "equivalent to principal" concept where the additional risk protection features of the security borrowing and lending agency arrangement are met. The effects of this revision are that:

   (a) the third party custodian agent would not need to be an acceptable institution in order for a Dealer Member to use the "equivalent to principal" concept,

because the margin requirements will be based on the counterparty type of the third party custodian agent and the additional risk protection features are not dependent on the third party custodian being an acceptable institution. The third party custodian agent would only need to meet the definition of "financial intermediary" contained in the Eligible Financial Contract General Rules (*Bankruptcy and Insolvency Act*). If the agency arrangement meets the criteria for "equivalent to principal" treatment, the Dealer Member would treat the agency arrangement as if it was an equivalent principal arrangement between the Dealer Member and the third party custodian agent and, as such, the reporting and margining of the arrangement would be based on the third party custodian agent's counterparty type. A summary of the margin impact is provided as Attachment F, and the definition of "financial intermediary" is available on the Justice Laws Website: http://laws-lois.justice.gc.ca/eng/regulations/SOR-2007-256/FullText.html;

(b) the underlying principal counterparty would not need to be an acceptable institution, acceptable counterparty or a regulated entity in order for a Dealer Member to use the "equivalent to principal" concept. A summary of the margin impact is provided as Attachment F;

(ii) revise the description of the default process in the additional written agreement requirement so that it more accurately describes one of the additional risk protection features of the security borrowing and lending agency arrangement that must be met, in order for a Dealer Member to use the "equivalent to principal" concept;

(iii) remove the explicit requirement that the securities borrowing and lending agreement must qualify as an "Eligible Financial Contract", because the definition of "Eligible Financial Contract" is general enough and includes securities, derivatives and margin related agreements—the definition of "Eligible Financial Contract" is available on the Justice Laws Website: http://laws-lois.justice.gc.ca/eng/regulations/SOR-2007-256/FullText.html;

(iv) clarify the margin requirements for each type of financing and securities borrowing and lending arrangement, by separating each arrangement and corresponding margin requirements, and more clearly distinguishing the requirements related to agency agreements, where an agent may be treated as equivalent to principal, from agency agreements where the agent must not be treated as equivalent to principal and how they are to be margined;

(v) clarify that the "equivalent to principal" concept only applies to certain securities borrowing and lending arrangements, and is not applicable to cash loans receivable or cash loans payable, which was the intent of the Original Proposal; and

(vi) make certain housekeeping amendments.

As revisions (i) through (iv) are considered to be material changes to the Original Proposal, the Proposed Amendments are being republished for a further comment period of 90 days.

Current rules

Background on cash/securities loan arrangements

A cash/securities loan is an agreement that is executed between a Dealer Member and another entity (the "counterparty"). The terms of the loan are governed by a loan agreement, which requires that the borrower provide the lender with collateral, in the form of cash or securities, of a value equal to or greater than the loaned cash/securities. Major lenders of securities include investment funds, insurance companies, pension plans and other large investment portfolios. Securities borrowing is an important tool used by hedge funds and other investment vehicles that follow a "short sale" strategy, to meet their transaction settlement obligations.

Current margin requirements

The current margin requirements for cash/securities loans allow Dealer Members to enter into such loans on:

- an unsecured basis with "acceptable institution"[2] counterparties;
- a modestly over-collateralized basis[3] with "acceptable counterparty"[4] counterparties;
- a "value for value" basis with "regulated entity"[5] counterparties; and
- a "loan value equivalency"[6] basis with "other"[7] counterparties

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[2] See Attachment E for a description of "acceptable institutions".

[3] Transactions that involve a modest amount of over-collateralization are transactions where the market value of the cash or securities provided as loan collateral by investment dealer is slightly in excess of the market value of the cash or securities received in by the investment dealer pursuant to the loan arrangement. Street practice is to require 102% over-collateralization when cash is provided as loan collateral and 105% over-collateralization when securities are provided as loan collateral.

[4] See Attachment E for a description of "acceptable counterparties".

[5] See Attachment E for a description of "regulated entities".

The effects of these margin requirements are to limit, in the case of a securities borrowing arrangement, the dollar amount of collateral that may be delivered by the borrower to the lending counterparty.

Concerns with current margin requirements

There are two concerns with the current margin requirements:

(i) the current rules do not set out specific margin requirements for agency cash and security borrowing and lending arrangements; and

(ii) the current rules do not impose the same margin requirements on cash and security borrowing and lending arrangements with "acceptable counterparty" versus "regulated entity" counterparties.

Agency agreements

Within the last year there has been a significant shift away from Dealer Members entering into cash and security borrowing and lending arrangements directly with the arrangement counterparty. Rather, the recent trend is for Dealer Members to execute an agency arrangement, whereby the Dealer Member enters into cash and security borrowing and lending arrangement with a third party custodian, who is acting as agent for the ultimate counterparty (also referred to as the underlying principal counterparty) to the arrangement. These agency arrangements have the following features:

- the third party custodian agent typically qualifies as an "acceptable institution" and administers an agency lending program on behalf of its clients;
- pursuant to the agency lending arrangements that are executed:
  - the loan collateral is held by the third party custodian agent and if the loan collateral includes securities the agent cannot re-hypothecate those securities;
  - in the event the Dealer Member defaults, the loan collateral that has been posted with the third party custodian agent will be liquidated by the third party custodian agent and the proceeds used to purchase the borrowed security, which will be returned to the underlying principal lender. If the borrowed security cannot be purchased in the market, its equivalent value is returned to the underlying principal

[6] Transactions performed on a "loan value equivalency" basis are those where the loan value of the cash or securities (which is market value less margin) received in by the investment dealer is equal to the loan value of the cash or securities delivered out by the investment dealer.

[7] See Attachment E for a description of "other" counterparties.

lender. Any excess value on the realization on the loan collateral will be returned by the third party custodian agent to the Dealer Member;

  - the agency agreement qualifies as an "Eligible Financial Contract" under Canadian legislation relating to bankruptcy, insolvency and creditor's rights, where the third party custodian agent meets the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (*Bankruptcy and Insolvency Act*), which means that the contract continues in the event that any party to the contract becomes insolvent, and the collateral does not form part of either the custodian's or the ultimate counterparty's estate in the event of an insolvency of either of them.

Given the features of these agency arrangements, IIROC staff have concluded that the risk assumed by a Dealer Member when entering into one of these arrangements is no greater than the risk assumed by a Dealer Member when entering directly into an equivalent "principal" arrangement with the third party custodian agent. Furthermore, there is an argument to be made that the risk is lower as the Dealer Member:

- will not have its collateral frozen, should the ultimate counterparty become insolvent; and
- will be able to quickly access its collateral, should the custodian become insolvent, because the agency lending arrangement qualifies as an "Eligible Financial Contract".

The current notes and instructions to Schedules 1 and 7 of Dealer Member Form 1 do not discuss these specific types of agency arrangements, nor do they recognize that the risk of such arrangements is equivalent to comparable "principal" arrangements. The result is that Dealer Members are required to "look through" the third party custodian agent to determine the entity that is the ultimate counterparty under the current IIROC margin rules, and provide additional margin for such arrangements in amounts that represent as much as 3% of the market value of the loan.

Different margin requirements for arrangements involving "acceptable counterparty" versus "regulated entity" counterparties

As a general rule, IIROC's rules allow Dealer Members to transact with other regulated dealers on a "value for value" basis, with mark to market imposed on outstanding transactions, without capital penalty. This general rule currently applies to all cash and security borrowing and lending arrangements between a Dealer Member and:

- another Dealer Member; and
- another dealer that qualifies as a "regulated entity", such as a FINRA dealer.

Notwithstanding this fact, it is now common street practice for Dealer Members to be asked to provide collateral with a value in excess of the amount of the loan when entering into cash and security borrowing and lending arrangements with regulated entities (i.e. other Dealer Members and foreign dealers).

The current IIROC rules that apply to cash and security borrowing and lending arrangements, where the counterparty is an "acceptable counterparty" allow for delivery of excess collateral representing between 102% and 105% of the amount of the loan without any margin implication. As credit risk exposures to "acceptable counterparties" and "regulated entities" are treated the same way for all other transactions, there is no risk-related reason why a modest amount of excess collateral should not be permitted for cash and security borrowing and lending arrangements where the counterparty is a "regulated entity", without similar margin relief. Without this relief, Dealer Members are required under the current IIROC margin rules to provide margin, that represents as much as 5% of the market value of the loan, in instances where a modest amount of over-collateralization is requested.

Proposed rules

To address the concerns with the current margin requirements, specifically that the current rules:

- do not set out specific margin requirements for agency cash and security borrowing and lending arrangements, and
- do not impose the same margin requirements on cash and security borrowing and lending arrangements with "acceptable counterparty" versus "regulated entity" counterparties,

the following amendments to that the Notes and Instructions to Schedules 1 and 7 and Schedule 7A of Dealer Member Form 1 are being proposed:

(i) Amend the definition of "excess collateral deficiency" that appears in Note 2 of the Notes and Instructions to Schedules 1 and 7, such that margin only applies when the collateral provided is in excess of:

   - 102% of the loan when the collateral provided is cash; and
   - 105% of the loan when the collateral provided is in the form of securities.

   In addition, the following **non-material revisions** have been added to the definition of "excess collateral deficiency" that appears in Note 2 of the Notes and Instructions to Schedules 1 and 7 to make the definition clearer:

- ““cash loans receivable” are loan transactions where the purpose of the loan is for the Dealer Member to lend cash and receive securities as collateral from the counterparty”;
- ““securities borrow arrangements” are loan transactions where the purpose of the loan is for the Dealer Member to borrow securities and deliver cash or securities as collateral to the counterparty”;
- ““cash loans payable” are loan transactions where the purpose of the loan is for the Dealer Member to borrow cash and deliver securities as collateral to the counterparty”; and
- ““securities loan arrangements” are loan transactions where the purpose of the loan is for the Dealer Member to lend securities and receive cash or securities as collateral from the counterparty”.

(ii) Introduce new Note 5(b) to the Notes and Instructions to Schedules 1 and 7 to specify the margin requirements for cash loans receivable and cash loans payable. In addition, the following **non-material revisions** to Note 5 to the Notes and Instructions to Schedules 1 and 7 have been made:

- for Schedule 1, the two arrangements “Cash loans receivable and securities borrowed arrangements” have been separated into “Cash loans receivable” and “Securities borrow arrangements” and “Securities borrow arrangements” will be in new Note 6 and the other subsequent Notes renumbered accordingly, each arrangement will have its own “Written agreement requirements”, “Additional written agreement requirements for certain agency agreements” (does not apply to cash loan receivable), “Margin requirements” in order to make the requirements for each arrangement clearer; and
- for Schedule 7, the two arrangements “Cash loans payable and securities loan arrangements” have been separated into “Cash loans payable” and “Securities loan arrangements” and “Securities loan arrangements” will be new Note 6 and the other subsequent Notes renumbered accordingly, each arrangement will have its own “Written agreement requirements”, “Additional written agreement requirements for certain agency agreements” (does not apply to cash loans payable), “Margin requirements” in order to make the requirements for each arrangement clearer.

(iii) The following **material revisions** have been made to new Note 6(b) to the Notes and Instructions to Schedules 1 and 7 with respect to the additional written

agreement requirements for certain agency agreements where the agent may be treated as equivalent to principal:

- remove the requirement for the third party custodian agent to qualify as an acceptable institution and the third party custodian agent's client (the underlying principal) to qualify as an acceptable institution, an acceptable counterparty, or a regulated entity, because qualifying agency securities borrowing and lending arrangements contain additional risk protection features that address the credit risk exposure associated with the third party custodian agent, and need not address the credit risk of the underlying principal client, and the margin requirements, irrespective of their counterparty types (below in new Note 6(c), have been revised to base the margin requirements on the counterparty type of the third party custodian agent for qualifying security borrowing and lending agency arrangements);
- remove the explicit requirement that the securities borrowing and lending agreement must qualify as an "Eligible Financial Contract", because the definition of "Eligible Financial Contract" is general enough and includes securities, derivatives and margin related agreements—the definition of "Eligible Financial Contract" is available on the Justice Laws Website: http://laws-lois.justice.gc.ca/eng/regulations/SOR-2007-256/FullText.html;
- limit the no re-hypothecation of collateral requirement to collateral provided in the form of securities, because it is normal market practice for third party custodian agents to use the cash it receives as collateral in its business.
- add the requirement that the third party custodian agent meets the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (*Bankruptcy and Insolvency Act*)—the definition of "financial intermediary" is available on the Justice Laws Website: http://laws-lois.justice.gc.ca/eng/regulations/SOR-2007-256/FullText.html;
- reword the description of the default process so that it more accurately describes one of the additional risk protection features of the security borrowing and lending agency arrangement that must be met; and
- add criteria to clarify when the agency arrangement must not be treated in the same manner as an equivalent principal arrangement between the Dealer Member and the custodian and, in those cases, how the agency arrangement is to be treated.

(iv) The following **material revision** has been made to new Note 6(c) to the Notes and Instructions to Schedules 1 and 7 with respect to margin requirements:

- add various situations in which an agency agreement could differ and include their corresponding treatment in order to clarify the margin requirements for agency security borrowing and lending arrangements under various situations.

(v) Amend note 7(b) to the Notes and Instructions to Schedules 1 and 7 to set "market value deficiency" as the standard margin requirement for resale and repurchase agreements involving "acceptable counterparties" and "regulated entities"—while the current rules do allow over-collateralization for certain resale and repurchase agreements involving "acceptable counterparties", IIROC Staff recommend that this margin requirement be revised from "excess collateral deficiency" to "market value deficiency" since:

- overcollateralization is not a common practice for repurchase and resale agreements; and
- allowing continued overcollateralization for repurchase and resale agreements would run counter to Bank of Canada's remarks on introducing "haircuts"[8] for these agreements in the near future.

(vi) Revise Schedule 7A to extend the existing overcollateralization concentration test, that currently only applies to overcollateralization exposures to "acceptable counterparties", to overcollateralization exposures to both "acceptable counterparties" and "regulated entities".

Issues and alternatives considered

Two alternatives were considered regarding the revisions to the Original Proposal, which include the alternative that was chosen. The first alternative, was to make any necessary non-material changes to clarify the intent and scope of application of the Original Proposal, and at a future date submit, as a separate proposal, amendments to expand the scope of the use of the "equivalent to principal" concept in order to apply it consistently where the additional risk protection features of the agency security borrowing and lending arrangement are met.

The second alternative, which was the alternative chosen, was to make any necessary material and non-material changes, including the material change to expand the scope of the use of the

[8] Shedding Light on Shadow Banking: http://www.bankofcanada.ca/2013/06/shedding-light-shadow-banking/

“equivalent to principal” concept in order to apply it consistently where the additional risk protection features of the agency security borrowing and lending arrangement are met.

Rule-making process

The Proposed Amendments were developed by IIROC Staff and recommended for approval by the FAS Capital Formula Subcommittee and the Financial Administrators Section, which are two IIROC policy advisory committees.

Comparison with similar provisions

Canada

Office of the Superintendent of Financial Institutions Canada

OSFI Guideline B-4 requires that lenders “should at all times hold adequate collateral to protect themselves against the risk associated with securities lending.” When the guideline was issued in September 1996 it stipulated that the level of collateral would be considered adequate if collateral of at least 105% of the market value of the securities lent was obtained. This requirement was changed in April 2007 to “at least 102 per cent” to accommodate situations where a borrower provides cash as collateral.

Canadian Securities Administrators

Section 2.12 of National Instrument 81-102, requires that mutual funds obtain collateral that represents “at least 102 percent” of the market value of the securities lent when lending securities. This requirement was based on the equivalent OSFI requirement set out in OSFI Guideline B-4.

United States

Rule 15c3-1(c)(2)(iv)(B)/09 of the Securities Exchange Act of 1934 requires that securities loan deficits exceeding 5% (equates to 105% over-collateralization) must be provided for in computing a dealers regulatory net capital. The rule does not distinguish between situations where the dealer has provides cash as loan collateral and situations where the dealer provides securities as loan collateral.

Proposed Rule classification

Statements have been made elsewhere as to the nature and effects of the Proposed Amendments, as well as analysis. The purpose of the Proposed Amendments is 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;*

- *foster fair, equitable and ethical business standards and practices; and*
- *promote the protection of investors.*

The Board therefore has determined that the Proposed Amendments are not contrary to the public interest.

Due to the extent and substantive nature of the Proposed Amendments, they have been classified as a Public Comment Rule proposal.

Effects of the proposed Rule on market structure, Dealer Members, non-Dealer Members, competition and costs of compliance

With the Proposed Amendments, Dealer Members will benefit from enhanced clarity and certainty in the calculation of credit risk margin and credit risk concentration margin for exposures resulting from the execution of cash and security borrowing and lending arrangements.

It is believed that the Proposed Amendments

(i) will have no impact in terms of capital market structure, competition generally, cost of compliance and conformity with other rules;

(ii) do not permit unfair discrimination among customers, issuers, brokers, dealers, members or others; and

(iii) do not impose any burden on competition that is not necessary or appropriate in furtherance of the above purposes.

Technological implications and implementation plan

There should not be significant technological implications for Dealer Members as a result of the Proposed Amendments. The Proposed Amendments will be implemented after their approval from the Recognizing Regulators within a reasonable period.

Request for public comment

Comments are sought on the Proposed Amendments. Comments should be made in writing. Two copies of each comment letter should be delivered by May 27, 2015 (90 days from the publication date of this notice). One copy should be addressed to the attention of:

Answerd Ramcharan
Specialist, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
Suite 2000, 121 King Street West

Toronto, ON M5H 3T9
aramcharan@iiroc.ca

The second copy should be addressed to the attention of:

Manager of Market Regulation
Ontario Securities Commission
19th Floor, Box 55
20 Queen Street West
Toronto, ON M5H 3S8
marketregulation@osc.gov.on.ca

Those submitting comment letters should be aware that a copy of their comment letter will be made publicly available on the IIROC website (**www.iiroc.ca** under the heading "Rulebook - IIROC Dealer Member Rules - Proposed Policy").

Questions may be referred to:

Answerd Ramcharan
Specialist, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
(416) 943-5850
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Attachments

Attachment A - Proposed amendments to Schedules 1, 7 and 7A [and related Notes and Instructions] of Dealer Member Form 1;

Attachment B - Black-line comparison of proposed amendments to Schedules 1, 7 and 7A [and related Notes and Instructions] of Dealer Member Form 1 to previously published proposal;

Attachment C - Black-line comparison of proposed amendments to Schedules 1, 7 and 7A [and related Notes and Instructions] of Dealer Member Form 1 to current Dealer Member Form 1;

Attachment D - IIROC Staffs' response to public comments received on previously published proposal; and

Attachment E - Discussion of four types of counterparties defined within IIROC's capital and margin rules; and

Attachment F - Summary of margin impact of the revisions to the previously published proposal.

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

MARGIN REQUIREMENTS FOR CERTAIN CASH AND SECURITY BORROWING AND LENDING ARRANGEMENTS – PROPOSED AMENDMENTS TO SCHEDULES 1, 7 AND 7A OF DEALER MEMBER FORM 1

TEXT OF THE PROPOSED AMENDMENTS

1. Dealer Member Form 1 is amended by repealing and replacing Schedules 1, 7 and 7A, and the Notes and Instructions thereto, with the following:

FORM 1, PART II – SCHEDULE 1

DATE: ____________________

____
(Dealer Member Name)

ANALYSIS OF LOANS RECEIVABLE, SECURITIES BORROWED AND RESALE AGREEMENTS

		AMOUNT OF LOAN RECEIVABLE OR CASH DELIVERED AS COLLATERAL C$'000 [see note 3]	MARKET VALUE OF SECURITIES DELIVERED AS COLLATERAL C$'000 [see note 4]	MARKET VALUE OF SECURITIES RECEIVED AS COLLATERAL OR BORROWED C$'000 [see note 4]	REQUIRED TO MARGIN C$'000
	LOANS RECEIVABLE:				
1.	*Acceptable institutions*		N/A		Nil
2.	*Acceptable counterparties*		N/A		
3.	*Regulated entities*		N/A		
4.	Others [see note 14]		N/A		
	SECURITIES BORROWED:				
5.	*Acceptable institutions*				Nil
6.	*Acceptable counterparties*				
7.	*Regulated entities*				
8.	Others [see note 14]				
	RESALE AGREEMENTS:				
9.	*Acceptable institutions*		N/A		Nil
10.	*Acceptable counterparties*		N/A		
11.	*Regulated entities*		N/A		
12.	Others [see note 14]		N/A		
13.	**TOTAL** [Lines 1 through 12]	A-6			B-9

FORM 1, PART II – SCHEDULE 1
NOTES AND INSTRUCTIONS

1. This schedule is to be completed for secured loan receivable transactions whereby the stated purpose of the transaction is to lend excess cash. All security borrowing and financing transactions done via 2 trade tickets, including resale transactions and those with related parties, should also be disclosed on this schedule.
2. For the purpose of this schedule,
   (a) "cash loans receivable" are loan transactions where the purpose of the loan is for the Dealer Member to lend cash and receive securities as collateral from the counterparty;
   (b) "excess collateral deficiency" is defined as:
      (i) For cash loans receivable, any excess of the amount of the loan over the market value of the actual collateral received from the transaction counterparty;

      or

      (ii) For securities borrow arrangements, any excess of the market value of the actual collateral provided to the transaction counterparty over:
         (A) 102% of the market value of the securities borrowed, where cash is provided as collateral; or
         (B) 105% of the market value of the securities borrowed, where securities are provided as collateral.

   and

   (c) "securities borrow arrangements" are loan transactions where the purpose of the loan is for the Dealer Member to borrow securities and deliver cash or securities as collateral to the counterparty.
3. Include accrued interest in amount of loan receivable.
4. Market value of securities delivered or received as collateral should include accrued interest.
5. **Cash loans receivable**

   (a) Written agreement requirements

   Any written agreement for a cash loan receivable between the Dealer Member and a counterparty must include terms which provide:
   (i) For the rights of either party to retain or realize on securities held by it from the other party on default;
   (ii) For events of default;
   (iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;
   (iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and
   (v) If set-off rights or security interests are created in securities provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

   (b) Margin requirements

   The margin requirements for a cash loan receivable are as follows:
   (i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 5(a), the margin required shall be:
      (A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the actual collateral provided to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 5(a),the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

6. **Securities borrow arrangements**

(a) Written agreement requirements

Any written agreement for a securities borrowing arrangement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default;

(ii) For events of default;

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

(v) If set-off rights or security interests are created in securities borrowed or securities provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

(b) Additional written agreement requirements for certain agency agreements

Agency agreements where agent may be treated as equivalent to principal

Any written collateral management or custodial agreement involving a securities borrowing arrangement between the Dealer Member and a third party custodian, which is acting as an agent, may be reported and treated in the same manner for margin purposes as the equivalent principal securities borrowing arrangement between the Dealer Member and the third party custodian, if all of the following additional terms [i.e. over and above those set out in Note 6(a)] are stipulated in the written agreement:

(i) the loan collateral must be held by the third party custodian agent and if the loan collateral is made up of securities there must be no right to re-hypothecate those securities;

(ii) in the event of the Dealer Member default, the loan collateral that has been posted with the third party custodian agent will be liquidated by the third party custodian agent and proceeds used to purchase the borrowed security which will be returned to the underlying principal lender. If the borrowed security cannot be purchased in the market, its equivalent value is returned to the underlying principal lender. Any excess value on the realization on the loan collateral will be returned by the third party custodian agent to the Dealer Member; and

(iii) the third party custodian agent must meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (Bankruptcy and Insolvency Act).

Agency agreements where agent must not be treated as equivalent to principal

Where these additional terms [(i),(ii) and (iii) immediately above] are not all present or the arrangement does not involve an agent that is acting as a third party custodian, the Dealer Member must look through the agent in the agency arrangement to the underlying principal lender and the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal securities borrowing arrangement between the Dealer Member and the underlying principal lender.

(c) Margin requirements

The margin requirements for a securities borrowing arrangement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 6(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the actual collateral provided to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 6(a), for margin purposes:

(A) For principal arrangements, the counterparty is the principal in the arrangement,

(B) For agency arrangements, where a third party custodian agent is involved and all of the additional required minimum terms in Note 6(b) are present, the counterparty is the third party custodian,

(C) For agency arrangements, where all of the additional required minimum terms in Note 6(b) are not present or the arrangement does not involve an agent that is acting as a third party custodian, the counterparty is the underlying principal lender,

the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

7. **Securities resale agreements**

(a) Written agreement requirements

Any written agreement for a securities resale agreement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default,

(ii) For events of default,

FORM 1, PART II – SCHEDULE 1
NOTES AND INSTRUCTIONS [Continued]

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party,

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority,

(v) If set-off rights or security interests are created in securities sold or loaned by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions; and

(vi) For an acknowledgement by the parties that either has the right, upon notice, to call for any shortfall in the difference between the collateral and the securities at any time.

(b) Margin requirements

The margin requirements for a securities resale agreement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required based on term of transaction	
	30 calendar days or less after regular settlement[1]	Greater than 30 calendar days after regular settlement[1]
Acceptable institution	No margin[2]	
Acceptable counterparty	Market value deficiency[2]	Margin
Regulated entity	Market value deficiency[2]	Margin
Other	Margin	200% of margin (to a maximum of the *market value* of the underlying securities)

[1] Regular settlement means the settlement date or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days refer to the original term of the resale transaction.

[2] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Market value deficiency[1]
Regulated entity	Market value deficiency[1]
Other	Margin

[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

8. For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.

FORM 1, PART II – SCHEDULE 1
NOTES AND INSTRUCTIONS [Continued]

9. In order for a pension fund to be treated as an *acceptable institution* for purposes of this Schedule, it must not only meet the *acceptable institution* criteria outlined in General Notes and Definitions, but the Dealer Member must also have received representation that the pension fund is legally able to enter into the obligations of the transaction. If such representation has not been received, the pension fund which otherwise meets the *acceptable institution* criteria must be treated as an *acceptable counterparty*.

10. **Lines 2, 3, 6 and 7 -** In the case of a cash loan receivable or a securities borrowing arrangement between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where an *excess collateral deficiency* exists, action must be taken to correct the deficiency. If no action is taken the amount of *excess collateral deficiency* must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

11. **Lines 10 and 11 -** In the case of a resale transaction between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where a deficiency exists between the *market value* of the securities resold and the *market value* of the cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of *market value* deficiency must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

12. **Lines 4, 8 and 12 -** In the case of a cash loan receivable or a securities borrowing or a resale arrangement / transaction between a Dealer Member and a party other than an *acceptable institution*, *acceptable counterparty* or *regulated entity*, where a deficiency exists between the loan value of the cash loaned or securities borrowed or resold and the loan value of the collateral or cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of loan value deficiency must be immediately provided out of the Dealer Member's capital. The margin required may be reduced by any margin already provided on the collateral (e.g. in inventory). Where the collateral is either held by the Dealer Member on a fully segregated basis or held in escrow on its behalf by an Acceptable Depository or a bank or trust company qualifying as either an *acceptable institution* or *acceptable counterparty*, only the amount of *market value* deficiency need be provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

13. **Lines 5, 6 and 7 -** In a securities borrowed transaction between a Dealer Member and an *acceptable institution*, *acceptable counterparty*, or *regulated entity*, where a letter of credit issued by a Schedule 1 Bank is used as collateral for the securities borrowed, there shall be no charge to the Dealer Member's capital for any excess of the value of the letter of credit pledged as collateral over the *market value* of the securities borrowed.

14. **Lines 4, 8 and 12 -** Arrangements other than those regarding agency agreements where an agent may be treated as equivalent to principal in Note 6(b) whereby an *acceptable institution*, *acceptable counterparty*, or *regulated entity* is only acting as an agent (on behalf of an "other" party) should be reported and margined as "Others".

FORM 1, PART II – SCHEDULE 7

DATE: ____________________

____
(Dealer Member Name)

ANALYSIS OF OVERDRAFTS, LOANS, SECURITIES LOANED AND REPURCHASE AGREEMENTS

	AMOUNT OF LOAN PAYABLE OR CASH RECEIVED AS COLLATERAL C$'000 [see note 3]	MARKET VALUE OF SECURITIES RECEIVED AS COLLATERAL C$'000 [see note 4]	MARKET VALUE OF SECURITIES DELIVERED AS COLLATERAL OR LOANED C$'000 [see note 4]	REQUIRED TO MARGIN C$'000
1. Bank overdrafts	________	N/A	N/A	Nil
LOANS PAYABLE:				
2. *Acceptable institutions*	________	N/A	________	Nil
3. *Acceptable counterparties*	________	N/A	________	________
4. *Regulated entities*	________	N/A	________	________
5. Others	________	N/A	________	________
SECURITIES LOANED:				
6. *Acceptable institutions*	________	________	________	Nil
7. *Acceptable counterparties*	________	________	________	________
8. *Regulated entities*	________	________	________	________
9. Others	________	________	________	________
REPURCHASE AGREEMENTS:				
10. *Acceptable institutions*	________	N/A	________	Nil
11. *Acceptable counterparties*	________	N/A	________	________
12. *Regulated entities*	________	N/A	________	________
13. Others	________	N/A	________	________
14. **TOTAL** [Lines 1 through 13]	________ A-51			________ B-14

[See notes and instructions]

FORM 1, PART II – SCHEDULE 7
NOTES AND INSTRUCTIONS

1. This schedule is to be completed for loan payable transactions, whereby the stated purpose of the transaction is to borrow cash. All security lending transactions and financing transactions done via 2 trade tickets, including securities repurchases and those with related parties, should also be disclosed on this schedule.
2. For the purpose of this schedule,
   (a) "cash loans payable" are loan transactions where the purpose of the loan is for the Dealer Member to borrow cash and deliver securities as collateral to the counterparty;
   (b) "excess collateral deficiency" is defined as:
      (i) For cash loans payable, any excess of the market value of the actual collateral delivered to the transaction counterparty over 102% the amount of the loan;

      or

      (ii) For securities loan arrangements, any excess of the market value of the securities loaned over the market value of securities or the amount of cash received from the transaction counterparty as collateral.

   and

   (c) "securities loan arrangements" are loan transactions where the purpose of the loan is for the Dealer Member to lend securities and receive cash or securities as collateral from the counterparty.
3. Include accrued interest in amount of loan payable.
4. Market value of securities received or delivered as collateral should include accrued interest.
5. **Cash loans payable**

   (a) Written agreement requirements

   Any written agreement for a cash loan payable between the Dealer Member and a counterparty must include terms which provide:
   (i) For the rights of either party to retain or realize on securities held by it from the other party on default;
   (ii) For events of default;
   (iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;
   (iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and
   (v) If set-off rights or security interests are created in securities provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

   (b) Margin requirements

   The margin requirements for a cash loan payable are as follows:
   (i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 5(a), the margin required shall be:
      (A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or
      (B) 100% of the market value of the actual collateral provided to the transaction counterparty.
   (ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 5(a),

the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

6. **Securities loan arrangements**

(a) Written agreement requirements

Any written agreement for a securities loan arrangement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default;

(ii) For events of default;

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

(v) If set-off rights or security interests are created in securities loaned or provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

(b) Additional written agreement requirements for certain agency agreements

Agency agreements where agent may be treated as equivalent to principal

Any written collateral management or custodial agreement involving a securities loan arrangement between the Dealer Member and a third party custodian, which is acting as an agent, may be reported and treated in the same manner for margin purposes as the equivalent principal securities loan arrangement between the Dealer Member and the third party custodian, if all of the following additional terms [i.e. over and above those set out in Note 6(a)] are stipulated in the written agreement:

(i) the loan collateral must be held by the third party custodian agent and if the loan collateral is made up of securities there must be no right to re-hypothecate those securities; and

(ii) in the event of the underlying principal borrower default, the loan collateral that has been posted with the third party custodian agent will be liquidated by the third party custodian agent and proceeds used to purchase the loaned security which will be returned to the Dealer Member. If the loaned security cannot be purchased in the market, its equivalent value is returned to the Dealer Member. Any excess value on the realization on the loan collateral will be returned by the third party custodian agent to the underlying principal borrower; and

(iii) the third party custodian agent must meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (Bankruptcy and Insolvency Act).

Agency agreements where agent must not be treated as equivalent to principal

Where these additional terms [(i),(ii) and (iii) immediately above] are not all present or the arrangement does not involve an agent that is acting as a third party custodian, the Dealer Member must look through the agent in the agency arrangement to the underlying principal borrower and the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal securities lending arrangement between the Dealer Member and the underlying principal borrower.

(c) Margin requirements

The margin requirements for a securities loan arrangement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 6(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the securities loaned to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 6(a), for margin purposes:

(A) For principal arrangements, the counterparty is the principal in the arrangement,

(B) For agency arrangements, where a third party custodian agent is involved and all of the additional required minimum terms in Note 6(b) are present, the counterparty is the third party custodian,

(C) For agency arrangements, where all of the additional required minimum terms in Note 6(b) are not present or the arrangement does not involve an agent that is acting as a third party custodian, the counterparty is the underlying principal borrower,

the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin

[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

7. **Securities repurchase agreements**

(a) Written agreement requirements

Any written agreement for a securities repurchase agreement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default,

(ii) For events of default,

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party,

FORM 1, PART II – SCHEDULE 7

NOTES AND INSTRUCTIONS [Continued]

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority,

(v) If set-off rights or security interests are created in securities sold or loaned by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions; and

(vi) For an acknowledgement by the parties that either has the right, upon notice, to call for any shortfall in the difference between the collateral and the securities at any time.

(b) Margin requirements

The margin requirements for a securities repurchase agreement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

	Margin required based on term of transaction	
Transaction counterparty type	**30 calendar days or less after regular settlement**[1]	**Greater than calendar 30 days after regular settlement**[1]
Acceptable institution	No margin[2]	
Acceptable counterparty	Market value deficiency[2]	Margin
Regulated entity	Market value deficiency[2]	Margin
Other	Margin	200% of margin (to a maximum of the *market value* of the underlying securities)

[1] Regular settlement means the settlement date or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days refer to the original term of the repurchase transaction.

[2] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Market value deficiency[1]
Regulated entity	Market value deficiency[1]
Other	Margin

[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

8. For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.

9. In order for a pension fund to be treated as an *acceptable institution* for purposes of this Schedule, it must not only meet the *acceptable institution* criteria outlined in General Notes and Definitions, but the Dealer Member must also have received representation that the pension fund is legally able to enter into the obligations of the transaction. If such

representation has not been received, the pension fund which otherwise meets the *acceptable institution* criteria must be treated as an *acceptable counterparty*.

10. **Lines 3, 4, 7 and 8 -** In the case of a cash loan payable or a securities loan arrangement between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where an *excess collateral deficiency* exists, action must be taken to correct the deficiency. If no action is taken, the amount of *excess collateral deficiency* must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day it must be provided out of the Dealer Member's capital.
11. **Lines 11 and 12 -** In the case of a repurchase transaction between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where a deficiency exists between the *market value* of the securities repurchased and the *market value* of the cash received, action must be taken to correct the deficiency. If no action is taken the amount of *market value* deficiency must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.
12. **Lines 5, 9 and 13 -** In the case of a cash loan payable or a securities loan or a repurchase arrangement / transaction between a Dealer Member and a party other than an *acceptable institution*, *acceptable counterparty* or *regulated entity*, where a deficiency exists between the loan value of the cash received or securities lent or repurchased and the loan value of the collateral or cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of loan value deficiency must be immediately provided out of the Dealer Member's capital. The margin required may be reduced by any margin already provided on the collateral (e.g. in inventory). Where the collateral is either held by the Dealer Member on a fully segregated basis or held in escrow on its behalf by an Acceptable Depository or a bank or trust company qualifying as either an *acceptable institution* or *acceptable counterparty*, only the amount of *market value* deficiency need be provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.
13. **Lines 2, 3 and 4 -** In a cash loan payable transaction between a Dealer Member and an *acceptable institution*, *acceptable counterparty*, or *regulated entity*, where a letter of credit issued by a Schedule 1 Bank is used as collateral for the cash loan, there shall be no charge to the Dealer Member's capital for any excess of the value of the letter of credit pledged as collateral over the cash borrowed.
14. **Lines 5, 9, and l3 -** Arrangements other than those regarding agency agreements where an agent may be treated as equivalent to principal in Note 6(b) whereby an *acceptable institution*, *acceptable counterparty*, or *regulated entity* is only acting as an agent (on behalf of an "other" party) should be reported and margined as "Others".

Attachment A

FORM 1, PART II – SCHEDULE 7A

DATE: ______________________

____
(Dealer Member Name)

CASH AND SECURITIES BORROWING AND LENDING ARRANGEMENTS CONCENTRATION CHARGE

			C$'000
1.	Sch. 1, Line 2	Market value deficiency amount relating to loans receivable from *acceptable counterparties*, net of legal offsets and margin already provided	
2.	Sch. 1, Line 3	Market value deficiency amount relating to loans receivable from *regulated entities*, net of legal offsets and margin already provided	
3.	Sch. 1, Line 6	Market value deficiency amount relating to securities borrowed from *acceptable counterparties*, net of legal offsets and margin already provided	
4.	Sch. 1, Line 7	Market value deficiency amount relating to securities borrowed from *regulated entities*, net of legal offsets and margin already provided	
5.	Sch. 7, Line 3	Market value deficiency amount relating to loans payable to *acceptable counterparties*, net of legal offsets and margin already provided	
6.	Sch. 7, Line 4	Market value deficiency amount relating to loans payable to *regulated entities*, net of legal offsets and margin already provided	
7.	Sch. 7, Line 7	Market value deficiency amount relating to securities lent to *acceptable counterparties*, net of legal offsets and margin already provided	
8.	Sch. 7, Line 8	Market value deficiency amount relating to securities lent to *regulated entities*, net of legal offsets and margin already provided	
9.		TOTAL MARKET VALUE DEFICIENCY EXPOSURE WITH ACCEPTABLE COUNTERPARTIES AND REGULATED ENTITIES, NET OF LEGAL OFFSETS AND MARGIN ALREADY PROVIDED [Sum of Lines 1 to 6]	
10.		CONCENTRATION THRESHOLD – 100% OF NET ALLOWABLE ASSETS	
11.		CONCENTRATION CHARGE [Excess of Line 9 over Line 10, otherwise NIL]	B-21

Attachment B

Investment Industry Regulatory Organization of Canada

Margin requirements for certain cash and security borrowing and lending arrangements – Proposed Amendments to Schedules 1, 7 and 7A of Dealer Member Form 1

Black-Line Comparison of Proposed Amendments to Previously Published Proposal

Attachment B

FORM 1, PART II – SCHEDULE 1

DATE: ______________________

____
(Dealer Member Name)

ANALYSIS OF LOANS RECEIVABLE, SECURITIES BORROWED AND RESALE AGREEMENTS

	AMOUNT OF LOAN RECEIVABLE OR CASH DELIVERED AS COLLATERAL C$'000 [see note 3]	MARKET VALUE OF SECURITIES DELIVERED AS COLLATERAL C$'000 [see note 4]	MARKET VALUE OF SECURITIES RECEIVED AS COLLATERAL OR BORROWED C$'000 [see note 4]	REQUIRED TO MARGIN C$'000
LOANS RECEIVABLE:				
1. *Acceptable institutions*		N/A		Nil
2. *Acceptable counterparties*		N/A		
3. *Regulated entities*		N/A		
4. Others [see note ~~13~~14]		N/A		
SECURITIES BORROWED:				
5. *Acceptable institutions*				Nil
6. *Acceptable counterparties*				
7. *Regulated entities*				
8. Others [see note ~~13~~14]				
RESALE AGREEMENTS:				
9. *Acceptable institutions*		N/A		Nil
10. *Acceptable counterparties*		N/A		
11. *Regulated entities*		N/A		
12. Others [see note ~~13~~14]		N/A		
13. **TOTAL** [Lines 1 through 12]				
	A-6			B-9

[See notes and instructions]

Attachment B

FORM 1, PART II – SCHEDULE 1
NOTES AND INSTRUCTIONS

1. This schedule is to be completed for secured loan receivable transactions whereby the stated purpose of the transaction is to lend excess cash. All security borrowing and financing transactions done via 2 trade tickets, including resale transactions and those with related parties, should also be disclosed on this schedule.

2. For the purpose of this schedule,

   (a) "cash loans receivable" are loan transactions where the purpose of the loan is for the Dealer Member to lend cash and receive securities as collateral from the counterparty;

   (b) "excess collateral deficiency" is defined as:

   (~~a~~i) For cash loans receivable, any excess of the amount of the loan over the market value of the actual collateral received from the transaction counterparty;

   or

   (~~b~~ii) For securities ~~borrowed~~borrow arrangements, any excess of the market value of the actual collateral provided to the transaction counterparty over:

   (~~i~~A) 102% of the market value of the securities borrowed, where cash is provided as collateral; or

   (~~ii~~B) 105% of the market value of the securities borrowed, where securities are provided as collateral.

   and

   (c) "securities borrow arrangements" are loan transactions where the purpose of the loan is for the Dealer Member to borrow securities and deliver cash or securities as collateral to the counterparty.

3. Include accrued interest in amount of loan receivable.

4. Market value of securities delivered or received as collateral should include accrued interest.

5. **Cash loans receivable ~~and securities borrowed arrangements~~**

   (a) Written agreement requirements

   Any written agreement for a cash loan receivable ~~or a securities borrowing arrangement~~ between the Dealer Member and a counterparty must include terms which provide:

   (i) For the rights of either party to retain or realize on securities held by it from the other party on default;

   (ii) For events of default;

   (iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

   (iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

   (v) If set-off rights or security interests are created in securities ~~sold or loaned~~provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

   (b~~) Additional written agreement requirements for agency agreements~~

   ~~Any written agreement for a cash loan receivable or a securities borrowing arrangement between the Dealer Member and an agent acting on the behalf of a counterparty, where:~~

   - ~~the agent qualifies as an *acceptable institution;*~~
   - ~~the counterparty qualifies as either an *acceptable institution,* an *acceptable counterparty* or a *regulated entity;*~~

must include the following additional terms [over and above those set out in Note 5(a)] which stipulate that:

(i) the loan collateral must be held by the agent without right to re-hypothecate; and

(ii) the loan collateral will only be made available to the counterparty when a Dealer Member default occurs and, if a default event occurs, any excess of the realization on the loan collateral over the loan repayment obligation will be returned to the Dealer Member.

Where these additional terms are not present or the agreement does not qualify as an "Eligible Financial Contract" in the event of the bankruptcy of any of the parties to the contract, the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal cash loan receivable or a securities borrowing arrangement between a Dealer Member and the same counterparty, where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms [Note 5(c)(i) below].

Where these additional terms are present and the agreement qualifies as an "Eligible Financial Contract" in the event of the bankruptcy of any of the parties to the contract, the agency arrangement may be reported and treated in the same manner for margin purposes as the equivalent principal cash loan receivable or a securities borrowing arrangement between a Dealer Member and the same counterparty [Note 5(c)(ii) below].**(c) Margin requirements**

The margin requirements for a cash loan receivable or a securities borrowing arrangement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 5(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the actual collateral provided to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 5(a), the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

6. **Securities borrow arrangements**

(a) Written agreement requirements

Any written agreement for a securities borrowing arrangement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default;

(ii) For events of default;

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

(v) If set-off rights or security interests are created in securities borrowed or securities provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

(b) Additional written agreement requirements for certain agency agreements

Agency agreements where agent may be treated as equivalent to principal

Any written collateral management or custodial agreement involving a securities borrowing arrangement between the Dealer Member and a third party custodian, which is acting as an agent, may be reported and treated in the same manner for margin purposes as the equivalent principal securities borrowing arrangement between the Dealer Member and the third party custodian, if all of the following additional terms [i.e. over and above those set out in Note 6(a)] are stipulated in the written agreement:

(i) the loan collateral must be held by the third party custodian agent and if the loan collateral is made up of securities there must be no right to re-hypothecate those securities;

(ii) in the event of the Dealer Member default, the loan collateral that has been posted with the third party custodian agent will be liquidated by the third party custodian agent and proceeds used to purchase the borrowed security which will be returned to the underlying principal lender. If the borrowed security cannot be purchased in the market, its equivalent value is returned to the underlying principal lender. Any excess value on the realization on the loan collateral will be returned by the third party custodian agent to the Dealer Member; and

(iii) the third party custodian agent must meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (Bankruptcy and Insolvency Act).

Agency agreements where agent must not be treated as equivalent to principal

Where these additional terms [(i),(ii) and (iii) immediately above] are not all present or the arrangement does not involve an agent that is acting as a third party custodian, the Dealer Member must look through the agent in the agency arrangement to the underlying principal lender and the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal securities borrowing arrangement between the Dealer Member and the underlying principal lender.

(c) Margin requirements

The margin requirements for a securities borrowing arrangement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 6(a), the margin required shall be:

  (A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

  (B) 100% of the market value of the actual collateral provided to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 6(a), for margin purposes:

  (A) For principal arrangements, the counterparty is the principal in the arrangement,

  (B) For agency arrangements, where a third party custodian agent is involved and all of the additional required minimum terms in Note 6(b) are present, the counterparty is the third party custodian,

(C) For agency arrangements, where all of the additional required minimum terms in Note 6(b) are not present or the arrangement does not involve an agent that is acting as a third party custodian, the counterparty is the underlying principal lender,

the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution, acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

7. **Securities resale agreements**

(a) Written agreement requirements

Any written agreement for a securities resale agreement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default,

(ii) For events of default,

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party,

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority,

(v) If set-off rights or security interests are created in securities sold or loaned by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions; and

(vi) For an acknowledgement by the parties that either has the right, upon notice, to call for any shortfall in the difference between the collateral and the securities at any time.

(b) Margin requirements

The margin requirements for a securities resale agreement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

	Margin required based on term of transaction	
Transaction counterparty type	**30 calendar days or less after regular settlement**[1]	**Greater than 30 calendar days after regular settlement**[1]
Acceptable institution	No margin[2]	
Acceptable counterparty	Market value deficiency[2]	Margin
Regulated entity	Market value deficiency[2]	Margin
Other	Margin	200% of margin (to a maximum of

		the *market value* of the underlying securities)

[1] Regular settlement means the settlement date or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days ~~refers~~refer to the original term of the resale transaction.

[2] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Market value deficiency[1]
Regulated entity	Market value deficiency[1]
Other	Margin

[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

~~7.~~8. For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.

~~8.~~9. In order for a pension fund to be treated as an *acceptable institution* for purposes of this Schedule, it must not only meet the *acceptable institution* criteria outlined in General Notes and Definitions, but the Dealer Member must also have received representation that the pension fund is legally able to enter into the obligations of the transaction. If such representation has not been received, the pension fund which otherwise meets the *acceptable institution* criteria must be treated as an *acceptable counterparty*.

~~9.~~10. **Lines 2, 3, 6 and 7 -** In the case of a cash loan receivable or a securities borrowing arrangement between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where an *excess collateral deficiency* exists, action must be taken to correct the deficiency. If no action is taken the amount of *excess collateral deficiency* must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

~~10.~~11. **Lines 10 and 11 -** In the case of a resale transaction between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where a deficiency exists between the *market value* of the securities resold and the *market value* of the cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of *market value* deficiency must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

~~11.~~12. **Lines 4, 8 and 12 -** In the case of a cash loan receivable or a securities borrowing or a resale arrangement / transaction between a Dealer Member and a party other than an *acceptable institution*, *acceptable counterparty* or *regulated entity*, where a deficiency exists between the loan value of the cash loaned or securities borrowed or resold and the loan value of the collateral or cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of loan value deficiency must be immediately provided out of the Dealer Member's capital. The margin required may be reduced by any margin already provided on the collateral (e.g. in inventory). Where the collateral is either held by the Dealer Member on a fully segregated basis or held in escrow on its behalf by an Acceptable Depository or a bank or trust company qualifying as either an *acceptable institution* or *acceptable counterparty*, only the amount of *market*

value deficiency need be provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

~~12.~~13. **Lines 5, 6 and 7 -** In a securities borrowed transaction between a Dealer Member and an *acceptable institution*, *acceptable counterparty*, or *regulated entity*, where a letter of credit issued by a Schedule 1 Bank is used as collateral for the securities borrowed, there shall be no charge to the Dealer Member's capital for any excess of the value of the letter of credit pledged as collateral over the *market value* of the securities borrowed.

~~13.~~14. **Lines 4, 8 and 12 -** Arrangements other than those ~~discussed in Note 5~~regarding agency agreements where an agent may be treated as equivalent to principal in Note 6(b) whereby an *acceptable institution*, *acceptable counterparty*, or *regulated entity* is only acting as an agent (on behalf of an "other" party) should be reported and margined as "Others".

Attachment B

FORM 1, PART II – SCHEDULE 7

DATE: ____________________

____
(Dealer Member Name)

ANALYSIS OF OVERDRAFTS, LOANS, SECURITIES LOANED AND REPURCHASE AGREEMENTS

		AMOUNT OF LOAN PAYABLE OR CASH RECEIVED AS COLLATERAL C$'000 [see note 3]	MARKET VALUE OF SECURITIES RECEIVED AS COLLATERAL C$'000 [see note 4]	MARKET VALUE OF SECURITIES DELIVERED AS COLLATERAL OR LOANED C$'000 [see note 4]	REQUIRED TO MARGIN C$'000
1.	Bank overdrafts		N/A	N/A	Nil
	LOANS PAYABLE:				
2.	*Acceptable institutions*		N/A		Nil
3.	*Acceptable counterparties*		N/A		
4.	*Regulated entities*		N/A		
5.	Others		N/A		
	SECURITIES LOANED:				
6.	*Acceptable institutions*				Nil
7.	*Acceptable counterparties*				
8.	*Regulated entities*				
9.	Others				
	REPURCHASE AGREEMENTS:				
10.	*Acceptable institutions*		N/A		Nil
11.	*Acceptable counterparties*		N/A		
12.	*Regulated entities*		N/A		
13.	Others		N/A		
14.	**TOTAL** [Lines 1 through 13]	A-51			B-14

[See notes and instructions]

Attachment B

FORM 1, PART II – SCHEDULE 7
NOTES AND INSTRUCTIONS

1. This schedule is to be completed for loan payable transactions, whereby the stated purpose of the transaction is to borrow cash. All security lending transactions and financing transactions done via 2 trade tickets, including securities repurchases and those with related parties, should also be disclosed on this schedule.

2. For the purpose of this schedule,

   (a) "cash loans payable" are loan transactions where the purpose of the loan is for the Dealer Member to borrow cash and deliver securities as collateral to the counterparty;

   (b) "excess collateral deficiency" is defined as:

   (~~a~~i) For cash loans payable, any excess of the market value of the actual collateral delivered to the transaction counterparty over 102% the amount of the loan;

   or

   (~~b~~ii) For securities ~~loaned~~loan arrangements, any excess of the market value of the securities loaned over the market value of securities or the amount of cash received from the transaction counterparty as collateral.

   and

   (c) "securities loan arrangements" are loan transactions where the purpose of the loan is for the Dealer Member to lend securities and receive cash or securities as collateral from the counterparty.

3. Include accrued interest in amount of loan payable.

4. Market value of securities received or delivered as collateral should include accrued interest.

5. **Cash loans payable ~~and securities loan arrangements~~**

   (a) Written agreement requirements

   Any written agreement for a cash loan payable ~~or a securities loan arrangement~~ between the Dealer Member and a counterparty must include terms which provide:

   (i) For the rights of either party to retain or realize on securities held by it from the other party on default;

   (ii) For events of default;

   (iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

   (iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

   (v) If set-off rights or security interests are created in securities ~~sold or loaned~~provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

   ~~**(b) Additional written agreement requirements for agency agreements**~~

   ~~Any written agreement for a cash loan payable or a securities loan arrangement between the Dealer Member and an agent acting on the behalf of a counterparty, where:~~

   - ~~the agent qualifies as an *acceptable institution*;~~
   - ~~the counterparty qualifies as either an *acceptable institution*, an *acceptable counterparty* or a *regulated entity*;~~

   ~~must include the following additional terms [over and above those set out in Note 5(a)] which stipulate that:~~

   ~~(i) the loan collateral must be held by the agent without right to re-hypothecate; and~~

~~(ii) the loan collateral will only be made available to the counterparty when a Dealer Member default occurs and, if a default event occurs, any excess of the realization on the loan collateral over the loan repayment obligation will be returned to the Dealer Member.~~

~~Where these additional terms are not present or the agreement does not qualify as an "Eligible Financial Contract" in the event of the bankruptcy of any of the parties to the contract, the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal cash loan payable or a securities loaned arrangement between a Dealer Member and the same counterparty where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms [Note 5(c)(i) below].~~

~~Where these additional terms are present and the agreement qualifies as an "Eligible Financial Contract" in the event of the bankruptcy of any of the parties to the contract, the agency arrangement may be reported and treated in the same manner for margin purposes as the equivalent principal cash loan payable or a securities loaned arrangement between a Dealer Member and the same counterparty [Note 5(c)(ii) below].~~

(~~c~~b) Margin requirements

The margin requirements for a cash loan payable ~~or a securities loan arrangement~~ are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 5(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the actual collateral provided to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 5(a), the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

6. **Securities loan arrangements**

(a) Written agreement requirements

Any written agreement for a securities loan arrangement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default;

(ii) For events of default;

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

(v) If set-off rights or security interests are created in securities loaned or provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

(b) Additional written agreement requirements for certain agency agreements

Agency agreements where agent may be treated as equivalent to principal

Any written collateral management or custodial agreement involving a securities loan arrangement between the Dealer Member and a third party custodian, which is acting as an agent, may be reported and treated in the same manner for margin purposes as the equivalent principal securities loan arrangement between the Dealer Member and the third party custodian, if all of the following additional terms [i.e. over and above those set out in Note 6(a)] are stipulated in the written agreement:

(i) the loan collateral must be held by the third party custodian agent and if the loan collateral is made up of securities there must be no right to re-hypothecate those securities; and

(ii) in the event of the underlying principal borrower default, the loan collateral that has been posted with the third party custodian agent will be liquidated by the third party custodian agent and proceeds used to purchase the loaned security which will be returned to the Dealer Member. If the loaned security cannot be purchased in the market, its equivalent value is returned to the Dealer Member. Any excess value on the realization on the loan collateral will be returned by the third party custodian agent to the underlying principal borrower; and

(iii) the third party custodian agent must meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (Bankruptcy and Insolvency Act).

Agency agreements where agent must not be treated as equivalent to principal

Where these additional terms [(i),(ii) and (iii) immediately above] are not all present or the arrangement does not involve an agent that is acting as a third party custodian, the Dealer Member must look through the agent in the agency arrangement to the underlying principal borrower and the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal securities lending arrangement between the Dealer Member and the underlying principal borrower.

(c) Margin requirements

The margin requirements for a securities loan arrangement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 6(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the securities loaned to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 6(a), for margin purposes:

(A) For principal arrangements, the counterparty is the principal in the arrangement,

(B) For agency arrangements, where a third party custodian agent is involved and all of the additional required minimum terms in Note 6(b) are present, the counterparty is the third party custodian,

(C) For agency arrangements, where all of the additional required minimum terms in Note 6(b) are not present

or the arrangement does not involve an agent that is acting as a third party custodian, the counterparty is the underlying principal borrower,

the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

7. Securities repurchase agreements

(a) Written agreement requirements

Any written agreement for a securities repurchase agreement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default,

(ii) For events of default,

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party,

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority,

(v) If set-off rights or security interests are created in securities sold or loaned by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions; and

(vi) For an acknowledgement by the parties that either has the right, upon notice, to call for any shortfall in the difference between the collateral and the securities at any time.

(b) Margin requirements

The margin requirements for a securities repurchase agreement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required based on term of transaction**	
	30 calendar days or less after regular settlement[1]	**Greater than calendar 30 days after regular settlement**[1]
Acceptable institution	No margin[2]	
Acceptable counterparty	Market value deficiency[2]	Margin
Regulated entity	Market value deficiency[2]	Margin
Other	Margin	200% of margin (to a maximum of the *market value* of the underlying

		securities)

[1] Regular settlement means the settlement date or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days ~~refers~~refer to the original term of the repurchase transaction.

[2] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Market value deficiency[1]
Regulated entity	Market value deficiency[1]
Other	Margin

[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

~~7.~~8. For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.

~~8.~~9. In order for a pension fund to be treated as an *acceptable institution* for purposes of this Schedule, it must not only meet the *acceptable institution* criteria outlined in General Notes and Definitions, but the Dealer Member must also have received representation that the pension fund is legally able to enter into the obligations of the transaction. If such representation has not been received, the pension fund which otherwise meets the *acceptable institution* criteria must be treated as an *acceptable counterparty*.

~~9.~~10. **Lines 3, 4, 7 and 8 -** In the case of a cash loan payable or a securities loan arrangement between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where an *excess collateral deficiency* exists, action must be taken to correct the deficiency. If no action is taken, the amount of *excess collateral deficiency* must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day it must be provided out of the Dealer Member's capital.

~~10.~~11. **Lines 11 and 12 -** In the case of a repurchase transaction between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where a deficiency exists between the *market value* of the securities repurchased and the *market value* of the cash received, action must be taken to correct the deficiency. If no action is taken the amount of *market value* deficiency must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

~~11.~~12. **Lines 5, 9 and 13 -** In the case of a cash loan payable or a securities loan or a repurchase arrangement / transaction between a Dealer Member and a party other than an *acceptable institution*, *acceptable counterparty* or *regulated entity*, where a deficiency exists between the loan value of the cash received or securities lent or repurchased and the loan value of the collateral or cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of loan value deficiency must be immediately provided out of the Dealer Member's capital. The margin required may be reduced by any margin already provided on the collateral (e.g. in inventory). Where the collateral is either held by the Dealer Member on a fully segregated basis or held in escrow on its behalf by an Acceptable Depository or a bank or trust company qualifying as either an *acceptable institution* or *acceptable counterparty*, only the amount of *market value* deficiency need be provided out of the Dealer Member's capital. In any case, where the deficiency exists for

FORM 1, PART II – SCHEDULE 7

NOTES AND INSTRUCTIONS [Continued]

more than one business day, it must be provided out of the Dealer Member's capital.

~~12.~~13. **Lines 2, 3 and 4 -** In a cash loan payable transaction between a Dealer Member and an *acceptable institution*, *acceptable counterparty*, or *regulated entity*, where a letter of credit issued by a Schedule 1 Bank is used as collateral for the cash loan, there shall be no charge to the Dealer Member's capital for any excess of the value of the letter of credit pledged as collateral over the cash borrowed.

~~13.~~14. **Lines 5, 9, and l3 -** Arrangements other than those ~~discussed in Note 5~~regarding agency agreements where an agent may be treated as equivalent to principal in Note 6(b) whereby an *acceptable institution*, *acceptable counterparty*, or *regulated entity* is only acting as an agent (on behalf of an "other" party) should be reported and margined as "Others".

FORM 1, PART II – SCHEDULE 7A

DATE: ____________________

____
(Dealer Member Name)

CASH AND SECURITIES BORROWING AND LENDING ARRANGEMENTS CONCENTRATION CHARGE

			C$'000
1.	Sch. 1, Line 2	Market value deficiency amount relating to loans receivable from *acceptable counterparties*, net of legal offsets and margin already provided	
2.	Sch. 1, Line 3	Market value deficiency amount relating to loans receivable from *regulated entities*, net of legal offsets and margin already provided	
3.	Sch. 1, Line 6	Market value deficiency amount relating to securities borrowed from *acceptable counterparties*, net of legal offsets and margin already provided	
4.	Sch. 1, Line 7	Market value deficiency amount relating to securities borrowed from *regulated entities*, net of legal offsets and margin already provided	
5.	Sch. 7, Line 3	Market value deficiency amount relating to loans payable to *acceptable counterparties*, net of legal offsets and margin already provided	
6.	Sch. 7, Line 4	Market value deficiency amount relating to loans payable to *regulated entities*, net of legal offsets and margin already provided	
7.	Sch. 7, Line 7	Market value deficiency amount relating to securities lent to *acceptable counterparties*, net of legal offsets and margin already provided	
8.	Sch. 7, Line 8	Market value deficiency amount relating to securities lent to *regulated entities*, net of legal offsets and margin already provided	
9.		TOTAL MARKET VALUE DEFICIENCY EXPOSURE WITH ACCEPTABLE COUNTERPARTIES AND REGULATED ENTITIES, NET OF LEGAL OFFSETS AND MARGIN ALREADY PROVIDED [Sum of Lines 1 to 6]	
10.		CONCENTRATION THRESHOLD – 100% OF NET ALLOWABLE ASSETS	
11.		CONCENTRATION CHARGE [Excess of Line 9 over Line 10, otherwise NIL]	B-21

Attachment C

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

MARGIN REQUIREMENTS FOR CERTAIN CASH AND SECURITY BORROWING AND LENDING ARRANGEMENTS – PROPOSED AMENDMENTS TO SCHEDULES 1, 7 AND 7A OF DEALER MEMBER FORM 1

BLACK-LINE COMPARISON OF PROPOSED AMENDMENTS TO CURRENT DEALER MEMBER FORM 1

Attachment C

FORM 1, PART II – SCHEDULE 1

DATE: ____________________

____
(Dealer Member Name)

ANALYSIS OF LOANS RECEIVABLE, SECURITIES BORROWED AND RESALE AGREEMENTS

	AMOUNT OF LOAN RECEIVABLE OR CASH DELIVERED AS COLLATERAL C$'000 [see note 3]	MARKET VALUE OF SECURITIES DELIVERED AS COLLATERAL C$'000 [see note 4]	MARKET VALUE OF SECURITIES RECEIVED AS COLLATERAL OR BORROWED C$'000 [see note 4]	REQUIRED TO MARGIN C$'000
LOANS RECEIVABLE:				
1. *Acceptable institutions*	__________	N/A	__________	Nil
2. *Acceptable counterparties*	__________	N/A	__________	__________
3. *Regulated entities*	__________	N/A	__________	__________
4. Others [see note ~~12~~14]	__________	N/A	__________	__________
SECURITIES BORROWED:				
5. *Acceptable institutions*	__________	__________	__________	Nil
6. *Acceptable counterparties*	__________	__________	__________	__________
7. *Regulated entities*	__________	__________	__________	__________
8. Others [see note ~~12~~14]	__________	__________	__________	__________
RESALE AGREEMENTS:				
9. *Acceptable institutions*	__________	N/A	__________	Nil
10. *Acceptable counterparties*	__________	N/A	__________	__________
11. *Regulated entities*	__________	N/A	__________	__________
12. Others [see note ~~12~~14]	__________	N/A	__________	__________
13. **TOTAL** [Lines 1 through 12]	__________ A-6			__________ B-9

[See notes and instructions]

FORM 1, PART II – SCHEDULE 1
NOTES AND INSTRUCTIONS

1. This schedule is to be completed for secured loan receivable transactions whereby the stated purpose of the transaction is to lend excess cash. All security borrowing ~~transactions and resale (i.e. reverse repo) agreements, including~~and financing transactions done via 2 trade tickets, including resale transactions and those with related parties, should also be disclosed on this schedule.

2. For the purpose of this schedule,

   (a) "cash loans receivable" are loan transactions where the purpose of the loan is for the Dealer Member to lend cash and receive securities as collateral from the counterparty;

   (b) "excess collateral deficiency" is defined as:

      (i) For cash loans receivable, any excess of the amount of the loan over the market value of the actual collateral ~~provided to the counterparty less the collateral required to be~~ received ~~by the counterparty pursuant to regulatory or legislative requirements. A list of current collateralization rates for each category of *acceptable counterparties* is published on a regular basis.~~from the transaction counterparty;

      or

      (ii) For securities borrow arrangements, any excess of the market value of the actual collateral provided to the transaction counterparty over:

         (A) 102% of the market value of the securities borrowed, where cash is provided as collateral; or

         (B) 105% of the market value of the securities borrowed, where securities are provided as collateral.

   and

   (c) "securities borrow arrangements" are loan transactions where the purpose of the loan is for the Dealer Member to borrow securities and deliver cash or securities as collateral to the counterparty.

3. Include accrued interest in amount of loan receivable.

4. Market value of securities delivered or received as collateral should include accrued interest.

5. ~~In the case of either a cash loan and securities borrowing or a resale transaction, if a~~**Cash loans receivable**

   (a) Written agreement requirements

      Any written agreement for a cash loan receivable between the Dealer Member and ~~the counterparty has been entered into containing the terms described below, the instructions in Notes 7, 8, 9, and 10 are applicable, as the case may be. Each such written agreement shall~~a counterparty must include terms which provide :

      (i) ~~for~~ For the rights of either party to retain or realize on securities held by it from the other party on default~~,~~ ;

      (ii) ~~for~~ For events of default~~,~~ ;

      (iii) ~~for~~ For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party~~;~~ ;

      (iv) ~~either~~ Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority~~,~~; and

      (v) ~~if~~ If set-off rights or security interests are created in securities ~~sold or loaned~~provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions. ~~In addition, in the case of a resale transaction such written agreement shall contain an acknowledgement by the parties that either has the right, upon notice, to call for any shortfall in the difference between the collateral and the securities at any time. Such agreements are not mandatory and if not used are to be margined as provided below.~~

FORM 1, PART II – SCHEDULE 1

NOTES AND INSTRUCTIONS [Continued]

(b) Margin requirements

~~In the case of~~The margin requirements for a cash loan ~~and securities borrowing transaction, if no such~~receivable are as follows:

(i) Where a written agreement has not been entered into ~~in respect of the transaction, then 100% of the *market value* must be provided as margin by the Dealer Member on the collateral given to the lender except in the case where the lender~~or the written agreement entered into does not include all of the required minimum terms in Note 5(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* ~~in which case no margin need be~~and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the actual collateral provided to the transaction counterparty.

~~In the case of a resale transaction, if no such~~(ii) Where a written agreement has been entered into ~~in respect~~that includes all of the ~~transaction, the position shall be margined as follows~~required minimum terms in Note 5(a),the margin required to be provided shall be determined according to the following table:

		~~**NO Written Repurchase/Reverse Repurchase Agreement Calendar days after regular settlement (Note 1)**~~	
~~**Counterparty**~~**Transaction counterparty type**	~~**Written Repurchase/Reverse Repurchase Agreement**~~**Margin required**	~~**30 days or less**~~	~~**Greater than 30 days**~~
Acceptable institution	No margin[1]		
Acceptable counterparty	Excess collateral deficiency[1]		
Regulated entity	~~Market~~Excess collateral deficiency[1]	~~Market deficiency (Note 2)~~	~~Margin~~
Other	Margin	~~Margin~~	~~200% of margin (to a maxi-mum of the *market value* of the underlying securities)~~
~~Note 1: Regular settlement means the settlement dates or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days refers to the original term of the repurchase/reverse repurchase.~~			
~~Note 2:~~[1]Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.			

6. ~~For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.~~**Securities borrow arrangements**

(a) Written agreement requirements

Any written agreement for a securities borrowing arrangement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default;

(ii) For events of default;

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

(v) If set-off rights or security interests are created in securities borrowed or securities provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

(b) Additional written agreement requirements for certain agency agreements

Agency agreements where agent may be treated as equivalent to principal

Any written collateral management or custodial agreement involving a securities borrowing arrangement between the Dealer Member and a third party custodian, which is acting as an agent, may be reported and treated in the same manner for margin purposes as the equivalent principal securities borrowing arrangement between the Dealer Member and the third party custodian, if all of the following additional terms [i.e. over and above those set out in Note 6(a)] are stipulated in the written agreement:

(i) the loan collateral must be held by the third party custodian agent and if the loan collateral is made up of securities there must be no right to re-hypothecate those securities;

(ii) in the event of the Dealer Member default, the loan collateral that has been posted with the third party custodian agent will be liquidated by the third party custodian agent and proceeds used to purchase the borrowed security which will be returned to the underlying principal lender. If the borrowed security cannot be purchased in the market, its equivalent value is returned to the underlying principal lender. Any excess value on the realization on the loan collateral will be returned by the third party custodian agent to the Dealer Member; and

(iii) the third party custodian agent must meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (Bankruptcy and Insolvency Act).

Agency agreements where agent must not be treated as equivalent to principal

Where these additional terms [(i),(ii) and (iii) immediately above] are not all present or the arrangement does not involve an agent that is acting as a third party custodian, the Dealer Member must look through the agent in the agency arrangement to the underlying principal lender and the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal securities borrowing arrangement between the Dealer Member and the underlying principal lender.

(c) Margin requirements

The margin requirements for a securities borrowing arrangement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 6(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the actual collateral provided to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 6(a), for margin purposes:

(A) For principal arrangements, the counterparty is the principal in the arrangement,

(B) For agency arrangements, where a third party custodian agent is involved and all of the additional required minimum terms in Note 6(b) are present, the counterparty is the third party custodian,

(C) For agency arrangements, where all of the additional required minimum terms in Note 6(b) are not present or the arrangement does not involve an agent that is acting as a third party custodian, the counterparty is the underlying principal lender,

the margin required to be provided shall be determined according to the following table:

7. **Lines 1, 5 and 9** - In a cash loan and securities borrow or resale transaction between a Dealer Member and an *acceptable institution*, no capital need be provided in the case where a deficiency exists between the *market value* of the cash loaned or securities borrowed or resold and the *market value* of the collateral or cash pledged.

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

7. Securities resale agreements

(a) Written agreement requirements

Any written agreement for a securities resale agreement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default,

(ii) For events of default,

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party,

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority,

(v) If set-off rights or security interests are created in securities sold or loaned by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions; and

(vi) For an acknowledgement by the parties that either has the right, upon notice, to call for any shortfall in the difference between the collateral and the securities at any time.

(b) Margin requirements

The margin requirements for a securities resale agreement are as follows:

FORM 1, PART II – SCHEDULE 1

NOTES AND INSTRUCTIONS [Continued]

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required based on term of transaction**	
	30 calendar days or less after regular settlement[1]	**Greater than 30 calendar days after regular settlement**[1]
Acceptable institution	No margin[2]	
Acceptable counterparty	Market value deficiency[2]	Margin
Regulated entity	Market value deficiency[2]	Margin
Other	Margin	200% of margin (to a maximum of the *market value* of the underlying securities)

[1] Regular settlement means the settlement date or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days refer to the original term of the resale transaction.

[2] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Market value deficiency[1]
Regulated entity	Market value deficiency[1]
Other	Margin

[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

8. For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.

9. In order for a pension fund to be treated as an *acceptable institution* for purposes of this Schedule, it must not only meet the *acceptable institution* criteria outlined in General Notes and Definitions, but the Dealer Member must also have received representation that the pension fund is legally able to enter into the obligations of the transaction. If such representation has not been received, the pension fund which otherwise meets the *acceptable institution* criteria must be treated as an *acceptable counterparty*.

~~WHERE AN AGREEMENT HAS BEEN EXECUTED, THEN:~~

~~8.~~10. **Lines 2, 3, 6 and ~~10~~7** - In the case of a cash loan ~~and~~receivable or a securities ~~borrow or resale transaction~~borrowing arrangement between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where an *excess collateral deficiency* exists, action must be taken to correct the deficiency. If no action is taken the amount of *excess collateral deficiency* must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

~~9.~~11. **Lines ~~3, 7~~10 and 11** - In the case of a ~~cash loan and securities borrow or~~ resale transaction between a Dealer

Member and either an *acceptable counterparty* or a *regulated entity*, where a deficiency exists between the *market value* of the ~~cash loaned or~~ securities ~~borrowed or~~ resold and the *market value* of the ~~collateral or~~ cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of *market value* deficiency must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

~~10.~~12. **Lines 4, 8 and 12 -** In the case of a cash loan ~~and~~receivable or a securities ~~borrow~~borrowing or a resale arrangement / transaction between a Dealer Member and a party other than an *acceptable institution*, *acceptable counterparty* or *regulated entity*, where a deficiency exists between the loan value of the cash loaned or securities borrowed or resold and the loan value of the collateral or cash pledged, action must be taken to correct the deficiency. If no action is taken the amount of loan value deficiency must be immediately provided out of the Dealer Member's capital. The margin required may be reduced by any margin already provided on the collateral (e.g. in inventory). Where the collateral is either held by the Dealer Member on a fully segregated basis or held in escrow on its behalf by an Acceptable Depository or a bank or trust company qualifying as either an *acceptable institution* or *acceptable counterparty*, only the amount of *market value* deficiency need be provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

~~11.~~13. **Lines 5, 6 and 7 -** In a securities borrowed transaction between a Dealer Member and an *acceptable institution*, *acceptable counterparty*, or *regulated entity*, where a letter of credit issued by a Schedule 1 Bank is used as collateral for the securities borrowed, there shall be no charge to the Dealer Member's capital for any excess of the value of the letter of credit pledged as collateral over the *market value* of the securities borrowed.

~~12.~~14. **Lines 4, 8 and 12 -** ~~Transactions~~Arrangements other than those regarding agency agreements where an agent may be treated as equivalent to principal in Note 6(b) whereby an *acceptable institution*, *acceptable counterparty*, or *regulated entity* ~~are~~is only acting as ~~agents~~an agent (on behalf of an "other" party) should be reported and margined as "Others".

Attachment C

FORM 1, PART II – SCHEDULE 7

DATE: ____________________

____
(Dealer Member Name)

ANALYSIS OF OVERDRAFTS, LOANS, SECURITIES LOANED AND REPURCHASE AGREEMENTS

	AMOUNT OF LOAN PAYABLE OR CASH RECEIVED AS COLLATERAL C$'000 [see note 3]	MARKET VALUE OF SECURITIES RECEIVED AS COLLATERAL C$'000 [see note 4]	MARKET VALUE OF SECURITIES DELIVERED AS COLLATERAL OR LOANED C$'000 [see note 4]	REQUIRED TO MARGIN C$'000
1. Bank overdrafts		N/A	N/A	Nil
LOANS PAYABLE:				
2. *Acceptable institutions*		N/A		Nil
3. *Acceptable counterparties*		N/A		
4. *Regulated entities*		N/A		
5. Others		N/A		
SECURITIES LOANED:				
6. *Acceptable institutions*				Nil
7. *Acceptable counterparties*				
8. *Regulated entities*				
9. Others				
REPURCHASE AGREEMENTS:				
10. *Acceptable institutions*		N/A		Nil
11. *Acceptable counterparties*		N/A		
12. *Regulated entities*		N/A		
13. Others		N/A		
14. **TOTAL** [Lines 1 through 13]	A-51			B-14

FORM 1, PART II – SCHEDULE 7
NOTES AND INSTRUCTIONS

1. This schedule is to be completed for loan payable transactions, whereby the stated purpose of the transaction is to borrow cash. All security lending transactions and ~~securities repurchases, including~~ financing transactions done via 2 trade tickets, including securities repurchases and those with related parties, should also be disclosed on this schedule.

~~2.~~ 2. For the purpose of this schedule,

(a) “cash loans payable” are loan transactions where the purpose of the loan is for the Dealer Member to borrow cash and deliver securities as collateral to the counterparty;

(b) "excess collateral deficiency" is defined as:

(i) For cash loans payable, any excess of the market value of the actual collateral ~~provided to the counterparty less the collateral required to be received by the counterparty pursuant to regulatory or legislative requirements. A list of current collateralization rates for each category of *acceptable counterparties* is published on a regular basis.~~ delivered to the transaction counterparty over 102% the amount of the loan;

or

(ii) For securities loan arrangements, any excess of the market value of the securities loaned over the market value of securities or the amount of cash received from the transaction counterparty as collateral.

and

(c) “securities loan arrangements” are loan transactions where the purpose of the loan is for the Dealer Member to lend securities and receive cash or securities as collateral from the counterparty.

~~3.~~ 3. Include accrued interest in amount of loan payable.

4. Market value of securities received or delivered as collateral should include accrued interest.

5. ~~In the case of either a cash borrow and securities loan or a repurchase transaction, if a~~ **Cash loans payable**

(a) Written agreement requirements

Any written agreement for a cash loan payable between the Dealer Member and ~~the counterparty has been entered into containing the terms described below, the instructions in Notes 7, 8, 9 and 10 are applicable, as the case may be. Each such written agreement shall~~ a counterparty must include terms which provide :

(i) ~~for~~ For the rights of either party to retain or realize on securities held by it from the other party on default~~,~~;

(ii) ~~for~~ For events of default~~,~~;

(iii) ~~for~~ For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party~~,~~;

(iv) ~~either~~ Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority~~,~~; and

(v) ~~if~~ If set-off rights or security interests are created in securities ~~sold or loaned~~ provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions. ~~In addition, in the case of a repurchase transaction such written agreement shall contain an acknowledgement by the parties that either has the right, upon notice, to call for any difference between the collateral and the securities at any time. Such agreements are not mandatory and if not used are to be margined as provided below.~~

(b) Margin requirements

~~In the case of~~ The margin requirements for a cash ~~borrow and securities loan transaction, if no such~~ loan payable are

as follows:

(i) Where a written agreement has not been entered into ~~in respect of the transaction, then 100% of the *market value* must be provided as margin by the Dealer Member on the collateral given to the lender except in the case where the lender~~or the written agreement entered into does not include all of the required minimum terms in Note 5(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* ~~in which case no margin need be~~and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the actual collateral provided to the transaction counterparty.

~~In the case of a repurchase transaction, if no such~~(ii) Where a written agreement has been entered into ~~in respect of the transaction, the position shall be margined as follows~~that includes all of the required minimum terms in Note 5(a), the margin required to be provided shall be determined according to the following table:

		~~**NO Written Repurchase/Reverse Repurchase Agreement Calendar days after regular settlement (Note 1)**~~	
~~**Counterparty**~~**Transaction counterparty type**	~~**Written Repurchase/Reverse Repurchase Agreement**~~**Margin required**	~~**30 days or less**~~	~~**Greater than 30 days**~~
Acceptable institution	No margin[1]		
Acceptable counterparty	Excess collateral deficiency[1]		
Regulated entity	~~Market~~Excess collateral deficiency[1]	~~Market deficiency (Note 2)~~	~~Margin~~
Other	Margin	~~Margin~~	~~200% of margin (to a maxi-mum of the *market value* of the underlying securities)~~
~~Note 1: Regular settlement means the settlement dates or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days refers to the original term of the repurchase/reverse repurchase.~~			
~~Note 2:~~[1]Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.			

6. ~~For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.~~**Securities loan arrangements**

(a) Written agreement requirements

Any written agreement for a securities loan arrangement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default;

(ii) For events of default;

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party;

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority; and

(v) If set-off rights or security interests are created in securities loaned or provided as collateral by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions.

(b) Additional written agreement requirements for certain agency agreements

Agency agreements where agent may be treated as equivalent to principal

Any written collateral management or custodial agreement involving a securities loan arrangement between the Dealer Member and a third party custodian, which is acting as an agent, may be reported and treated in the same manner for margin purposes as the equivalent principal securities loan arrangement between the Dealer Member and the third party custodian, if all of the following additional terms [i.e. over and above those set out in Note 6(a)] are stipulated in the written agreement:

(i) the loan collateral must be held by the third party custodian agent and if the loan collateral is made up of securities there must be no right to re-hypothecate those securities; and

(ii) in the event of the underlying principal borrower default, the loan collateral that has been posted with the third party custodian agent will be liquidated by the third party custodian agent and proceeds used to purchase the loaned security which will be returned to the Dealer Member. If the loaned security cannot be purchased in the market, its equivalent value is returned to the Dealer Member. Any excess value on the realization on the loan collateral will be returned by the third party custodian agent to the underlying principal borrower; and

(iii) the third party custodian agent must meet the definition of “financial intermediary” in relation to the Eligible Financial Contract General Rules (Bankruptcy and Insolvency Act).

Agency agreements where agent must not be treated as equivalent to principal

Where these additional terms [(i),(ii) and (iii) immediately above] are not all present or the arrangement does not involve an agent that is acting as a third party custodian, the Dealer Member must look through the agent in the agency arrangement to the underlying principal borrower and the agency arrangement must be reported and treated in the same manner for margin purposes as the equivalent principal securities lending arrangement between the Dealer Member and the underlying principal borrower.

(c) Margin requirements

The margin requirements for a securities loan arrangement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms in Note 6(a), the margin required shall be:

(A) Nil, where the counterparty to the transaction is an *acceptable institution* and the transaction has been confirmed with the *acceptable institution*, or

(B) 100% of the market value of the securities loaned to the transaction counterparty.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms in Note 6(a), for margin purposes:

(A) For principal arrangements, the counterparty is the principal in the arrangement,

(B) For agency arrangements, where a third party custodian agent is involved and all of the additional required minimum terms in Note 6(b) are present, the counterparty is the third party custodian,

(C) For agency arrangements, where all of the additional required minimum terms in Note 6(b) are not present or the arrangement does not involve an agent that is acting as a third party custodian, the counterparty is the underlying principal borrower,

the margin required to be provided shall be determined according to the following table:

7. **Lines 2, 6, and 10 -** In a cash borrowed and securities loan or repurchase transaction between a Dealer Member and an *acceptable institution*, no capital need be provided in the case where a deficiency exists between the *market value* of the cash borrowed or securities loaned or repurchased and the *market value* of the collateral or cash pledged.

Transaction counterparty type	**Margin required**
Acceptable institution	No margin[1]
Acceptable counterparty	Excess collateral deficiency[1]
Regulated entity	Excess collateral deficiency[1]
Other	Margin
[1] Any transaction which has not been confirmed by an *acceptable institution*, *acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.	

7. **Securities repurchase agreements**

(a) Written agreement requirements

Any written agreement for a securities repurchase agreement between the Dealer Member and a counterparty must include terms which provide:

(i) For the rights of either party to retain or realize on securities held by it from the other party on default,

(ii) For events of default,

(iii) For the treatment of the value of securities held by a non-defaulting party in excess of amounts which may be owed by a defaulting party,

(iv) Either for set-off or, in the case of secured loans of securities, continuous segregation of collateral and the requirement for the lender to perfect a security interest in collateral giving the highest priority,

(v) If set-off rights or security interests are created in securities sold or loaned by one party to another, that the securities are endorsed for transfer, where applicable, and free of any trading restrictions; and

(vi) For an acknowledgement by the parties that either has the right, upon notice, to call for any shortfall in the difference between the collateral and the securities at any time.

(b) Margin requirements

The margin requirements for a securities repurchase agreement are as follows:

(i) Where a written agreement has not been entered into or the written agreement entered into does not include all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

NOTES AND INSTRUCTIONS [Continued]

Transaction counterparty type	Margin required based on term of transaction	
	30 calendar days or less after regular settlement[1]	Greater than calendar 30 days after regular settlement[1]
Acceptable institution	No margin[2]	
Acceptable counterparty	Market value deficiency[2]	Margin
Regulated entity	Market value deficiency[2]	Margin
Other	Margin	200% of margin (to a maximum of the *market value* of the underlying securities)

[1] Regular settlement means the settlement date or delivery date generally accepted according to industry practice for the relevant security in the market in which the transaction occurs. Margin is calculated from the date of regular settlement. Calendar days refer to the original term of the repurchase transaction.

[2] Any transaction which has not been confirmed by an *acceptable institution, acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

(ii) Where a written agreement has been entered into that includes all of the required minimum terms, the margin required to be provided shall be determined according to the following table:

Transaction counterparty type	Margin required
Acceptable institution	No margin[1]
Acceptable counterparty	Market value deficiency[1]
Regulated entity	Market value deficiency[1]
Other	Margin

[1] Any transaction which has not been confirmed by an *acceptable institution, acceptable counterparty* or *regulated entity* within 15 business days of the trade shall be margined.

8. For any given counterparty a deficiency in one type of loan may be offset by an excess in another type of loan provided that there are written agreements for each type of loan which provide for the right of offset between each type of loan. In such case, the balances may also be offset for margin calculation purposes.

9. In order for a pension fund to be treated as an *acceptable institution* for purposes of this Schedule, it must not only meet the *acceptable institution* criteria outlined in General Notes and Definitions, but the Dealer Member must also have received representation that the pension fund is legally able to enter into the obligations of the transaction. If such representation has not been received, the pension fund which otherwise meets the *acceptable institution* criteria must be treated as an *acceptable counterparty*.

~~WHERE AN AGREEMENT HAS BEEN EXECUTED, THEN:~~

~~8.~~10. **Lines 3, ~~7,~~4, 7 and ~~11~~8** - In the case of a cash ~~borrowed and~~loan payable or a securities loan ~~or repurchase transaction~~arrangement between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where an *excess collateral deficiency* exists, action must be taken to correct the deficiency. If no action is taken, the amount of *excess collateral deficiency* must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day it must be provided out of the Dealer Member's capital.

~~9.~~11. **Lines ~~4, 8,~~11 and 12** - In the case of a ~~cash borrowed and securities loan or~~ repurchase transaction between a Dealer Member and either an *acceptable counterparty* or a *regulated entity*, where a deficiency exists between the *market value* of the ~~cash borrowed or~~ securities ~~loaned or~~ repurchased and the *market value* of the ~~collateral or~~ cash ~~pledged~~received, action must be taken to correct the deficiency. If no action is taken~~,~~ the amount of *market value*

deficiency must be immediately provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

10.12. **Lines 5, 9,9 and I313 -** In the case of a cash borrowed andloan payable or a securities loan or a repurchase arrangement / transaction between a Dealer Member and a party other than an *acceptable institution*, *acceptable counterparty* or *regulated entity*, where a deficiency exists between the loan value of the cash borrowedreceived or securities loanedlent or repurchased and the loan value of the collateral or cash pledged, action must be taken to correct the deficiency. If no action is taken, the amount of loan value deficiency must be immediately provided out of the Dealer Member's capital. The margin required may be reduced by any margin already provided on the collateral (e.g. in inventory). Where the collateral is either held by the Dealer Member on a fully segregated basis or held in escrow on its behalf by an Acceptable Depository or a bank or trust company qualifying as either an *acceptable institution* or *acceptable counterparty*, only the amount of *market value* deficiency need be provided out of the Dealer Member's capital. In any case, where the deficiency exists for more than one business day, it must be provided out of the Dealer Member's capital.

11.13. **Lines 2, 3 and 4 -** In a cash borrowedloan payable transaction between a Dealer Member and an *acceptable institution*, *acceptable counterparty*, or *regulated entity*, where a letter of credit issued by a Schedule 1 Bank is used as collateral for the cash borrowedloan, there shall be no charge to the Dealer Member's capital for any excess of the value of the letter of credit pledged as collateral over the cash borrowed.

12.14. **Lines 5, 9, and I3 -** TransactionsArrangements other than those regarding agency agreements where an agent may be treated as equivalent to principal in Note 6(b) whereby an *acceptable institution*, *acceptable counterparty*, or *regulated entity* areis only acting as agentsan agent (on behalf of an "other" party) should be reported and margined as "Others".

Attachment C

FORM 1, PART II – SCHEDULE 7A

DATE: ____________________

____
(Dealer Member Name)

~~ACCEPTABLE COUNTERPARTIES FINANCING ACTIVITIES~~CASH AND SECURITIES BORROWING AND LENDING ARRANGEMENTS CONCENTRATION CHARGE

			C$'000
1.	Sch. 1, Line 2	Market value deficiency amount relating to loans receivable from *acceptable counterparties*, net of legal offsets and margin already provided	
2.	Sch. 1, Line ~~6~~3	Market value deficiency amount relating to ~~securities borrowed from *acceptable counterparties*~~loans receivable from *regulated entities*, net of legal offsets and margin already provided	
3.	Sch. 1, Line ~~10~~6	Market value deficiency amount relating to ~~resale agreements with~~securities borrowed from *acceptable counterparties*, net of legal offsets and margin already provided	
4.	Sch. ~~7,~~1, Line ~~3~~7	Market value deficiency amount relating to ~~loans payable to *acceptable counterparties*~~securities borrowed from *regulated entities*, net of legal offsets and margin already provided	
5.	Sch. 7, Line ~~7~~3	Market value deficiency amount relating to ~~securities lent~~loans payable to *acceptable counterparties*, net of legal offsets and margin already provided	
6.	Sch. 7, Line ~~11~~4	Market value deficiency amount relating to ~~repurchase agreements with *acceptable counterparties*~~loans payable to *regulated entities*, net of legal offsets and margin already provided	
7.	Sch. 7, Line 7	Market value deficiency amount relating to securities lent to *acceptable counterparties*, net of legal offsets and margin already provided	
8.	Sch. 7, Line 8	Market value deficiency amount relating to securities lent to *regulated entities*, net of legal offsets and margin already provided	
~~7.~~9.		TOTAL MARKET VALUE DEFICIENCY EXPOSURE WITH ACCEPTABLE COUNTERPARTIES AND REGULATED ENTITIES, NET OF LEGAL OFFSETS AND MARGIN ALREADY PROVIDED [Sum of Lines 1 to 6]	
~~8.~~10.		CONCENTRATION THRESHOLD – 100% OF NET ALLOWABLE ASSETS	
~~9.~~11.		~~FINANCING ACTIVITIES~~ CONCENTRATION CHARGE [Excess of Line ~~7~~9 over Line ~~8,~~10, otherwise NIL]	

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Public comments and IIROC Staff response

Comment #	Public comment	IIROC Staff response
1.	**<u>Security Borrowing/Lending Agency Agreements where Agent is an AI</u>** In the situation where the Agent qualifies as an AI and the member has a written securities borrowing/lending agreement which includes all of the terms required in a standard borrowing agreement (see 5a per the guidance), how should the capital requirements for AC/RE and "Other" underlying clients be calculated? Per the revised guidance, it appears that you need to provide capital equal to 100% of the collateral delivered. Have we interpreted this guidance correctly? It seems very punitive, especially for AC/RE counterparties. *[TD Securities]*	The proposed amendments were not intended to make the capital requirements for security borrowing and lending arrangements more punitive than the current capital requirements for these arrangements. In the situation where the Agent qualifies as an AI and the Dealer Member has a written securities borrowing/lending agreement which includes all of the terms required in a standard borrowing agreement (i.e. all the requirements in Note 5(a) are met), but not all the requirements in Note 5(b) are met, the capital requirements would be based on the counterparty classification of the underlying client (i.e. the dealer would look through the Agent). Therefore, the capital requirements for AC/RE and "Other" underlying clients would be calculated as follows: • AC/RE, the margin required is excess overcollateralization amount; and • Other, the margin required is loan value deficiency amount. We have made revisions to the original proposal and clarified that you do not need to provide capital equal to 100% of the collateral delivered for the situation described above.
2.	**<u>Non-AI Agents</u>** While the revised rules address the situation where the Agent qualifies as an AI, members will benefit from explicit rules that address the situation where an Agent does <u>not</u> qualify as an AI.	We agree that Dealer Members would benefit from explicit rules to address the situation where an Agent does <u>not</u> qualify as an AI, and have made the necessary revisions to the original proposal. In addition, the revisions would apply the "equivalent

Comment #	Public comment	IIROC Staff response
	It would be beneficial if there was added guidance for each of the situations where the underlying clients are AI's, AC/RE's and "Other", where the agent it not an AI. Furthermore, if the Agent does not qualify as an AI, do we require the additional terms listed in 5b (see revised guidance) to be included in the agency agreement? If yes what are the capital requirements where the clauses in 5b are missing from the agreement for each of the situations for each of the situations where the underlying clients are AI's, AC's/RE's and "Other". *[TD Securities]*	to principal" concept consistently to any Agent where the additional risk protection features are present in an agency security borrowing and lending arrangement. If the agency security borrowing and lending arrangement meets the criteria for "equivalent to principal" treatment the Dealer Member would treat the agency arrangement as if it was a principal arrangement between the Dealer Member and the Agent. As a result, the reporting and margining of the arrangement would be based on the counterparty classification of the Agent. We have clarified in the revisions to the original proposal that the additional terms listed in Note 5(b) of the original proposal are only necessary if the "equivalent to principal" concept is to going to be used by the Dealer Member. The revisions to the original proposal clarify that if the additional terms are not present then the Dealer Member must look through the Agent and treat the agency arrangement as if it was an equivalent principal arrangement between the Dealer Member and the underlying principal lender and use the counterparty classification of the underlying principal lender for reporting and margining purposes.
3.	**Eligible Financial Contracts** Would it be considered appropriate to assume that members' securities borrowing agreements are considered to be "Eligible Financial Contracts" if the agreements follow the IIROC agreement "template" for security borrowing/lending arrangements? Are there any other clauses that must be embedded in the agreements to ensure that the agreements qualify as "Eligible Financial Contracts"? It would be greatly	Yes, based on the definition of "Eligible Financial Contracts" it would be considered appropriate to assume that Dealer Member's securities borrowing agreements are considered to be "Eligible Financial Contracts" if the agreement follows the IIROC standard industry agreements for security borrowing and lending arrangements. The definition of "Eligible Financial Contracts" can be found on the Justice Laws Website: http://laws-lois.justice.gc.ca/eng/regulations/SOR-2007-

Comment #	Public comment	IIROC Staff response
	beneficial if the guidance could provide more detail with respect to what exactly constitutes an "Eligible Financial Contract". *[TD Securities]*	256/FullText.html. In the revisions to the original proposal we have removed the explicit requirement that the securities borrowing and lending agreement must qualify as an "Eligible Financial Contract", because the definition of "Eligible Financial Contract" is general enough and includes securities, derivatives and margin related agreements. However, in the revisions to the original proposal for an agency securities borrowing and lending arrangement to be treated as if it was an equivalent principal arrangement between the Dealer Member and the Agent, the Agent must meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (*Bankruptcy and Insolvency Act*). That definition can be also be found on the Justice Laws Website: http://laws-lois.justice.gc.ca/eng/regulations/SOR-2007-256/FullText.html.
4.	Generally, Casgrain supports IIROC's proposed Amendments, which will align overcollateralization rates with today's current market practice and US regulation, establish a specific margin framework for securities borrowed transactions conducted through agency arrangements and recognize that the risk for such agency arrangements is no greater than entering into a comparable arrangement directly with the arrangement counterparty (as principal). Casgrain appreciates IIROC's initiative and effort for considering the current trend in the securities lending market i.e. the change in Custodians' business model from a principal model to an agency model, standardizing margin requirements amongst counterparties and supporting an efficient capital market. *[Casgrain & Company Limited]*	[No response required.]

Comment #	Public comment	IIROC Staff response
5.	**<u>Cash Loans Receivable and Securities Borrowed Arrangements - Additional Written Agreement Requirements for Agency Agreements</u>** We are questioning the reasons underlying the necessity for more stringent requirements for securities borrowed transactions conducted through agency agreements compared to securities borrowed arrangements conducted on a principal basis directly with a counterparty type such as AC, RE or other, and more particularly with AC and other counterparty types not subject to regulatory or legislative oversight. Moreover, there is no assurance that Agent Lenders will amend their current agency agreements with Members to incorporate the new IIROC written requirements. We believe that the current written terms and conditions prescribed in Rule 2200 sufficiently address credit and market exposure risks for any type of counterparties involved in security loan transactions. Our understanding of the proposed rule change was to set out a specific margin framework for agency arrangements as under IIROC current rules, it is not set it out other than by guidance and to level the playing field and over-collateralization rates with market practices and regulatory or legislative overcollateralization requirements. Under the current margin model for securities borrowing, we understand that additional requirements may have been warranted to regulate security loan transactions conducted through an Agent Lender. However, now that IIROC's over-collateralization framework proposal is extended to all AC and RE counterparty types, regardless of the fact that over-collateralization is required or	The proposed amendments were not intended to make the capital requirements for security borrowing and lending arrangements more punitive than the current capital requirements for these arrangements. The more stringent requirements (i.e. the additional requirements in Note 5(b)) for securities borrowed transactions conducted through agency agreements are necessary risk protection features if the Dealer Member wants to treat the agency arrangement as if it was an equivalent principal arrangement between the Dealer Member and Agent. As detailed in our response to Comment #2, we have clarified in the revisions to the original proposal that if the additional terms are not present in the agency securities borrowing agreement, that the Dealer Member is to look through the Agent and treat the agency arrangement as if it was an equivalent principal arrangement between the Dealer Member and the underlying principal lender.

Comment #	Public comment	IIROC Staff response
	not by regulatory or legislative requirements, some of the additional term requirements are no longer necessary. We do not foresee Members having higher exposure to credit exposure for transactions conducted on an agency basis where the counterparty is either AC, RE or other than if such transactions would have been conducted directly on a principal basis with the counterparty type itself. *[Casgrain & Company Limited]*	
6.	**<u>Cash Loans Receivable and Securities Borrowed Arrangements - Additional Written Agreement Requirements for Agency Agreements</u>** Therefore, we recommend that the proposed additional requirements to be imposed for agency arrangements be removed. • If the above proposal is not retained, we seriously recommend that the following be considered: i) One of the additional written requirements necessitates that the loan collateral must be held by the agent without right to re-hypothecate. Although this is common practice where <u>securities</u> are provided as collateral, the same cannot be said where <u>cash</u> is provided as collateral. Where cash is provided as collateral, it may never be subject to continuous segregation or the right to not rehypothecate or transfer. It is generally understood and as a general market practice, if such collateral consists of cash, the Agent Lender may at its own risk or on behalf of its counterparty clients use or invest the collateral; the	i) In the revisions to the original proposal, we have made the change to limit the "no right to re-hypothecate" requirement to securities that are provided as collateral for agency securities borrowing and lending agreements where the agreement can be treated as if it was an equivalent principal arrangement between the Dealer Member and the Agent. ii) Although the holding of securities without the right to re-hypothecate is currently market practice, we believe it is an essential risk protection feature that must be in an agency agreement in order for the Dealer Member to treat the arrangement as if it was an equivalent principal arrangement with the Agent. Regarding IIROC Rule 2200.2(c)—"For the treatment of the value of securities or collateral held by the non-defaulting party that is in excess of the amount owed by the defaulting party"—we believe the additional default related requirement in the proposal is an essential risk protection feature that must be in an agency agreement in order for the Dealer Member to treat the agency arrangement as if it was an equivalent principal

Comment #	Public comment	IIROC Staff response
	purpose is to allow the Lender Agent to generate a return higher than the one offered to Members on the cash collateral, which should technically correspond to the minimum loan fees charged to Members if non-cash collateral would have been provided. We therefore recommend that such requirements be revisited and limited to non-cash collateral. ii) The condition regarding the holding of non-cash collateral without right to re-hypothecate is currently a market practice and we believe there is no need to reiterate in writing what is already a market practice. With regards to the condition for the treatment of any excess of the realization on the loan collateral over the loan repayment obligation, it addresses only in the event of member defaults, [which is already a current condition that must be present in all securities loan agreement Rule 2200.2 (c)], and not the opposite, i.e. in the event of an Agent Lender counterparty default. A provision which addresses the treatment of the excess collateral held by the Agent Lender over the loan repayment obligation {i.e. for the overcollateralization amount) in the event of an Agent Lender's counterparty should perhaps be considered. iii) If any of the additional requirements is not satisfied, Members will be in a worse position in terms of capital requirements, and will be required to provide a margin corresponding to 100% of the market value of the collateral provided rather than the excess collateral deficiency as currently required. We caution IIROC to	arrangement with the Agent. iii) As detailed in our response to Comment #1, the proposed amendments were not intended to make the capital requirements for security borrowing and lending arrangements more punitive than the current capital requirements for these arrangements. In addition, the revisions to the original proposal clarify our intended margin treatment when the additional terms in Note 5(b) are not met. iv) We were referring to the agency agreement as a financial agreement for the purpose of the definition of "Eligible Financial Contract" in section 2 of the *Bankruptcy and Insolvency Act*. In our revisions to the original proposal, we have removed the explicit requirement that the securities borrowing and lending agreement must qualify as an "Eligible Financial Contract", because the definition of "Eligible Financial Contract" is general enough and includes securities, derivatives and margin related agreements.

Comment #	Public comment	IIROC Staff response
	consider the impacts on member dealer business and capital (especially where cash collateral is provided), including but not limited to, unduly restricting Members' ability to finance their inventory positions, limiting their business, and overstating credit exposure risk resulting in higher capital requirements. iv) Schedules 1 and 7 Notes and Instructions refer to whether the agreement does not qualify as an Eligible Financial Contract in the event of a bankruptcy. Are we referring to the agreement itself as opposed to the security loans themselves? Or both? If such, to minimize confusion, we suggest that IIROC be more specific. In addition, as there are no standard agency agreements (agreements may differ from Agent Lenders to Agent Lenders and from Members to Members), does IIROC intend to provide guidance where an agreement does not qualify as an Eligible Financial Contract or should Members obtain a legal opinion or similar confirmation of such? The Eligible Financial Contract definition "an agreement to borrow or lend securities" under the Bankruptcy and Insolvency Act, is broad enough. As a result, we do not foresee any securities loan agreements which would not qualify as an Eligible Financial Contract. *[Casgrain & Company Limited]*	
7.	**Cash Loans Payable and Securities Loan Arrangements - Additional Written Requirements for Agency Arrangements**	In the revisions to the original proposal we have separated cash loans payable from securities loan arrangements and also clarified that the "equivalent to principal" concept is for only certain agency securities borrow arrangements and agency

Comment #	Public comment	IIROC Staff response
	• We seek clarification on the applicability of such principles <u>in the context of agency loans payable and securities loan arrangements</u>. These Agents Lenders are providers of securities (not borrowers of securities) and do not lend cash (instead they receive cash as collateral). We have difficulty in determining situations where such transactions can occur. *[Casgrain & Company Limited]*	securities loan arrangements. Although, these Agent Lenders are currently providers of securities (not borrower of securities) we have provided requirements for the reverse situations in case a Dealer Member may want to lend securities through an Agent Borrower.
8.	**<u>General Comments Regarding Written Agreement Requirements for Each Type of Financing Transactions Arrangements</u>** • Schedule 1 and 7 Notes and Instructions describe the minimum written requirements for each type of financial transaction arrangements (securities loans, reverse repos/repos, etc.). However, we notice that amongst the written requirements for a specific financing arrangement type, some terms and conditions also refer to another type of financing arrangement for which it is not applicable. For example, there is a reference to the concept of securities sold (condition V) in the written agreement requirements for cash loan receivables and securities borrowed arrangements while we refer to secured loans or loaned securities in the resale agreement written requirements (conditions IV and V). To minimize potential confusion and to enhance clarity, we recommend that the written agreement requirements be tailored to each type of financing arrangements.	• In the revisions to the original proposal, we have separated cash loans receivable from securities borrow arrangements, and cash loans payable and securities loan arrangements in order to clarify the applicable written agreement requirements and the corresponding margin requirements. • In the revisions to the original proposal, as suggested we have added the words “where applicable”.

Comment #	Public comment	IIROC Staff response
	• Moreover, we also recommend to add the word "where applicable" in the fifth condition of each written agreement requirement section after the words "that the securities are endorsed for transfer and free of any trading restrictions" to reflect that the securities are now generally settled though the CDSX system (in BEO form). *[Casgrain & Company Limited]*	
9.	**<u>Securities Resale/Repurchase Agreements</u>** • In the context of margin requirements where a written agreement has not been entered into or does not contain the minimum requirements, we seek clarification for the purpose of adding the concept of "after regular settlement". There is no such concept of "regular settlement" for resale/repurchase transaction. This concept relates more specifically to providing margin for clients and regulated entities on extended settlement trading transactions than for resale/repurchase transactions. In addition, in Rule 100.17 which addresses term risk for resale/repo transactions, there is no such concept. • Consideration should also be given as to whether similar margin treatment regarding the overcollateralization be awarded for resale/repurchase agreements. We recognize that it may counter the Bank of Canada's proposal to introduce "haircut" for resale/repurchase agreements, but overcollateralization is becoming more and more imposed by counterparties, including member dealers although it is not a general common practice for the time being. In	• For securities resale agreements, the concept of “after regular settlements” is used in current the Notes and Instructions to Schedule 1 and is not an added concept in the original proposal. Similarly, for securities repurchase agreements, the concept of “after regular settlements” is used in the current Notes and Instructions to Schedule 7 and is not a new concept that has been added to the original proposal. The purpose of the concept “after regular settlement” and “regular settlement” is to establish when margin is to be calculated. • Should overcollateralization with respect to securities resale agreements and securities repurchase agreements become an industry concern in the future we will revisit that issue at that time.

Comment #	Public comment	IIROC Staff response
	substance, resale/repurchase transactions bear remarkable resemblance to security loans collateralized by cash and both can be used as alternative means for financing purposes. Accordingly, depending on the method chosen to finance its activities. Members may be subject to different margin requirements, even though the end result would be the same. Allowing different margin standards may have unintentional impacts on the repo and securities lending markets and therefore we suggest further consultation on this concept. • Further, we note that in the U.S., over-collateralization is allowed for repos only. SEC Rule 15c3-l (c) (2) (iv) (F) (3) requires that only the repo deficit in excess of an over-collateralization rate (each based on a category of security, as established in the Rule) be provided as a capital charge. *[Casgrain & Company Limited]*	
10.	We appreciate IIROC's support in quickly addressing and implementing the changes to margin requirements which are outlined in the Notice. The response time in granting investment dealer relief for "excess collateral deficiency" in their dealings with certain Acceptable Counterparties was done in a very efficient and expedited manner; however we propose the following changes to the Notice to better reflect the securities lending market currently: 1. **Description of Collateral** - Background on cash/securities loan arrangements (pp.2-3) The borrower may provide the lender with various forms of	1. **Description of Collateral** For margin purposes, we refer to collateral as either cash or securities and believe this to be the appropriate reference, because cash or securities are the main classes of assets we allow to be used as collateral for cash and security borrowing and lending arrangements. 2. **Canadian Bankruptcy Rules** In the revisions to the original proposal, we have removed the explicit requirement that the agency securities borrowing and lending agreement must qualify as an

Comment #	Public comment	IIROC Staff response
	collateral in order to complete the securities lending transaction. The list that is provided on the top of page 3 is not complete. We suggest IIROC simply refer to the collateral as "cash or non-cash collateral" in order to ensure that all forms of collateral are captured in this description. 2. **Canadian Bankruptcy Rules** - Agency Lending (pp.4-5) In the discussion of how risk is actually lower for Dealer Members who participate in agency transactions, we propose the following clarification: "Further, there is an argument to be made that the risk is lower as the Dealer Member: • Will not have its collateral frozen should the ultimate counterparty become insolvent; and • Will be able to quickly access its collateral should the custodian become insolvent, provided that the agency lending arrangement qualifies as an "*Eligible Financial Contract" and the lender is considered a "Financial Institution under Canadian insolvency statues.*" *[The Canadian Securities Lending Association (CASLA)]*	"Eligible Financial Contract", because the definition of "Eligible Financial Contract" is general enough and includes securities, derivatives and margin related agreements. In addition, we have added the requirement that the third party custodian agent (i.e. the Agent) must meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (*Bankruptcy and Insolvency Act*).
11.	Finally, CASLA would welcome further dialogue with IIROC on the categorization and limits prescribed for various entities defined within IIROC's capital and margin rules in Attachment C of the Notice. We believe that there is a need to update the limits and/or descriptions of counterparty clients to better reflect current participants in the Canadian securities lending market.	Although, we believe the categorization and limits prescribed for various entities defined within IIROC's capital and margin rules in Attachment C of the Notice (i.e. IIROC's counterparty classification—"acceptable counterparties", "acceptable institutions", "regulated entities", "Other")—have worked well in our capital formula regulatory framework over the years—we are open to assessing whether those categories and limits

Comment #	Public comment	IIROC Staff response
	[The Canadian Securities Lending Association (CASLA)]	continue to support the effective management of counterparty credit risk.
12.	We applaud IIROC in taking swift action to examine these important issues. We are grateful for the immediate relief IIROC granted for Agency Lending Agreements where the lending client is AC, AI or RE. We would ask IIROC to extend the same treatment where the client is "Other".[1] [[1] The terms AC, AI, RE and Others have the meanings given to those terms in IIROC's capital and margin rules and discussed in Attachment C of IIROC's proposal. For brevity, in our response we refer to AC, AI and RE as "AC, AI" and Others as "Other".] Our view is consistent with IIROC's statement that the type of counterparty (AC, AI or Other) was never considered under the principal arrangement and, for the reasons explained below, we believe the same should be true under an agency arrangement. We agree strongly with IIROC that there is an argument to be made that the risk is lower for broker dealer (BD) borrowers with the move to an agency model. The points below expand on our reasoning. **EXCLUDING OTHERS FROM FAVOURABLE CAPITAL TREATMENT IS UNNECESSARY** We believe that the typical Agency Lending Agreement BDs sign with Agents mitigate against concerns IIROC may have about the creditworthiness of the Agent's ultimate lender client. The Agency Lending Agreement would typically include language that ensures the agent does not have the right to re-	We have made revisions to the original proposal. These revisions apply the "equivalent to principal" concept consistently where the additional risk protection features of the security borrowing and lending agency arrangement are met. The effects of these revision are: (a) the third party custodian agent would not need to be an acceptable institution in order for a Dealer Member to use the "equivalent to principal" concept. The third party custodian agent would need to meet the definition of "financial intermediary" in relation to the Eligible Financial Contract General Rules (*Bankruptcy and Insolvency Act*). If the agency arrangement meets the criteria for "equivalent to principal" treatment the Dealer Member would treat the agency arrangement as if it was a principal arrangement between the Dealer member and the third party custodian agent, and the reporting and margining of the arrangement would be based on the counterparty classification of the third party custodian agent; and (b) the underlying principal counterparty would not need to be an acceptable institution, acceptable counterparty, or a regulated entity in order for a Dealer Member to use the "equivalent to principal" concept.

Comment #	Public comment	IIROC Staff response
	hypothecate the loan collateral posted by the borrower.[2] In this respect, the Agency Lending Agreement provides the same protections to the BD borrower in respect of a principal lender that is Other as well as AC or AI. [[2] The points in this section are in essence also noted in IIROC's proposal in the section titled "Agency agreements" (pgs. 4-5)] **The loan collateral that brokers pledge to "Others" is held in a segregated account by the Agent in the same manner (title transfer) as ACs and AIs.** As noted above, typically with an Agency Lending Agreement an Agency lender will have no re-hypothecation rights to the loan collateral. This means the assets remain in escrow at the Agent and are accessible to the BD lender. **In the case of an "Other's" default, the broker's collateral is as secure as with ACs or AIs.** The workout process would be the same regardless of whether the lending principal is an AC, AI, or Other. Securities lending transactions are generally eligible financial contracts under Canadian insolvency law. Accordingly, there is minimal risk that the insolvent estate of the underlying securities lender or its creditors would have access to the BD's collateral or be able to delay the exercise of the borrower's contractual remedies under the Agency Lending Agreement. Regardless of the end client's creditworthiness, the same steps would be taken by the borrower following the insolvency of the lender, regardless of whether it is AC, AI or Other.	

Comment #	Public comment	IIROC Staff response
	Following the insolvency of a lending principal, the BD would have the right to declare an Event of Default and terminate the affected loans. Title to the BD's collateral will have passed to the lender however the lender still has an obligation to return "Equivalent Collateral" to the borrower. The BD would either return Equivalent Securities against redelivery of the Equivalent Collateral from the Agent, or liquidate the borrowed securities and use the proceeds to buy-in replacement collateral. Since the Agent is prohibited by contract from re-hypothecating the collateral, the Agent should be in a position to return this collateral swiftly to the BD. *[CIBC World Markets Inc.]*	
13.	**IMPACT ASSESSMENT** **The risks of not extending the same treatment to Others is significant** By not extending the same treatment to Others, IIROC's proposed amendments will have a significant impact on both independent BDs and Bank-owned BDs in terms of capital market structure over time. These impacts could affect capital costs and the competitiveness of the Canadian marketplace generally. As an overall concern for Canada we note that significant changes in relative value will always drive behavioural change on the part of market participants. **The higher capital costs in Canada are expected to drive BD and investor activity away from Canada and into foreign jurisdictions.**	Please refer to our response to Comment #12.

Comment #	Public comment	IIROC Staff response
	For Bank-owned BDs subject to Basel III, regulatory capital requirements are reshaping the landscape in terms of with whom and how BDs will trade with the market. The expensive IIROC capital treatment for "Others" will amplify the effect of Basel III on Canadian Bank-owned BDs.[3] [[3] Basel III requirements are driving the trend in Canada away from principal-based custodial lending to "as agent" custodial lending. We expect that trend to continue.] Higher capital costs will constrain BD activity with Others or result in higher fees being passed on to investors. Overall activity levels, as well as liquidity, in Canadian equity finance would face significant headwinds as a result of higher costs. Additionally, Canadian BDs might feel compelled to seek alternative non-Canadian principal based lenders for their required supply. **Administrative burden** With the trend moving towards agency agreements the increased administrative burden on BDs to assess the creditworthiness of the Agent's lending clients is also significant. We estimate the annual cost to be on average three hours of work per year to review and maintain a record for each account. Canadian BDs must now conduct thousands of these reviews per year. **FINAL THOUGHTS** In sum, the Agency Lending Agreement protections are the same and the BD's recourse is the same regardless of whether	

Comment #	Public comment	IIROC Staff response
	the end client is AC, AI or Other. If IIROC does not extend capital treatment to Others, there is a risk that the Canadian marketplace can expect to see reduced supply, higher fees and BDs migrating to transact with non-Canadian principal lenders. *[CIBC World Markets Inc.]*	
14.	**1. Alignment of Margin Requirements** RBCDS is supportive of the IIROC initiative to align the margin requirements for cash and securities borrowing and lending arrangements for counterparties that are regulated entities ("RE") with the requirements for acceptable counterparties ("AC") and to clearly define "excess collateral deficiency". The proposed amendments will better reflect current business and risk management practices. *[RBC Dominion Securities Inc. (RBC DS)]*	No response required.
15.	**2. Agency Arrangement for Cash and Securities Borrowing and Lending Arrangements - Note 5(b) of Schedules 1 and 7, Part II of IIROC Form 1** We welcome IIROC's intention to formalize the application of the same margin requirements for certain qualifying agency cash and securities borrowing and lending arrangements as for the equivalent principal arrangement. The proposed note 5(b) regarding Agency Agreements only addresses situations where the agent qualifies as an acceptable institution ("AI"). We request guidance from IIROC on what margin requirements would apply when the third party agent qualifies as an Acceptable Counterparty.	Regarding the margin requirements for agency security borrowing and lending arrangements when the third party custodian agent qualifies as an acceptable counterparty, please see our response to Comment #2 and Comment #12. Regarding the clarification of the scope of the requirement, we have made the following revisions: **"(b) Additional written agreement requirements for certain agency agreements** **Agency agreements where agent may be treated as equivalent to principal** Any written collateral management or custodial agreement ~~for a cash loan receivable or~~involving a

Comment #	Public comment	IIROC Staff response
	While note 5(b) refers to written agreements involving an "agent acting on behalf of a counterparty" based on commentary in Notice 14-0066 it appears that the objective of the proposal is to address a situation where a third party custodian is acting as a custodian for the Dealer Member and counterparty ("tri-party arrangement") rather than an agency arrangement where no custodian is used. To clarify the scope of the requirement, we suggest that the proposed provision be revised as follows: "Any written collateral management or custodial agreement involving ~~for~~ a cash loan receivable or a securities borrowing arrangement between the Dealer Member and a~~n~~ third party custodian ~~agent acting on behalf of a counterparty~~, where: […]" *[RBC Dominion Securities Inc. (RBC DS)]*	securities borrowing arrangement between the Dealer Member and a third party custodian, which is acting as an agent ~~acting on the behalf of a counterparty, where~~, may be reported and treated in the same manner for margin purposes as the equivalent principal securities borrowing arrangement between the Dealer Member and the third party custodian, if all of the following additional terms [i.e. over and above those set out in Note 6(a)] are stipulated in the written agreement: …"
16.	Further, the proposal to require the additional terms noted in 5(b)(i) and (ii) ("additional terms") regarding re-hypothecation and excess of the realization on the loan collateral in Agency Agreements is not compatible with the way existing master agreements work nor with current business practices: (i) Where a Dealer Member enters into a master agreement with an agent acting on behalf of an underlying principal or principals, the agent does not hold collateral. Collateral flows directly from underlying principal to Dealer Member and vice versa, as if it were a bilateral agreement between the underlying principal and the Dealer Member. The standard master agreement is a "title transfer" agreement, which means	(i) Regarding the scenario in which the agent does not hold collateral, we have clarified the scope of our requirement to limit the "equivalent to principal" concept to where the agent is a third party custodian agent, as detailed in our response to Comment #15. Therefore, the agent must hold the collateral in certain agency agreements where the third party custodian agent may be treated as equivalent to principal. Regarding the written requirement that may inadvertently constrain the ability of the agent lender to re-hypothecate cash collateral, we have made the following revisions to the original proposal to correct this:

Comment #	Public comment	IIROC Staff response
	title to the collateral is transferred from one party to the other. As outright owner of the collateral, the party who receives it may re-hypothecate the collateral. Where the parties to a cash loan or securities lending arrangement enter into a tri-party arrangement with a custodian, the custodian holds the collateral on behalf of the Dealer Member/principal. The custodial/collateral management agreement between the parties provides that the transferee of the collateral is the owner of the collateral and has full control over the collateral. The custodian does not have any rights to use or re-hypothecate the collateral belonging to either the Dealer Member or the counterparty. Consequently, the addition of a restriction on re-hypothecation to either the existing agency master agreements or the custody/collateral management agreements is redundant with respect to a third party custodian and conflicts with the title transfer mechanism inherent to the standard master documentation for this type of transaction. Additionally, agent lenders require the ability to re-hypothecate cash as this an integral part of their financing service. The proposed written term as drafted may inadvertently constrain the ability of agent lenders to re-hypothecate cash collateral. (ii) We request additional clarification from IIROC on the reasoning behind the addition of the term specifying the return of any excess of the realization on the loan in the event of a default. Under a standard principal lending agreement the collateral belongs to the counterparty to whom it is transferred in exchange for the loan, until such time as the loan is repaid. The use of a third party custodian as agent does not change the	“(i) the loan collateral must be held by the ~~agent without~~third party custodian agent and if the loan collateral is made up of securities there must be no right to re-hypothecate those securities;~~ and~~” (ii) It is our understanding that with respect to agency security borrowing transactions, that are within scope of our “equivalent to principal” treatment, in the event of a Dealer Member default, the default process would be as follows and we have made revisions to the original proposal accordingly: “(ii) in the event of the Dealer Member default, the loan collateral that has been posted with the third party custodian agent will ~~only be made available to the counterparty when a Dealer Member default occurs and, if a default event occurs, any excess of~~be liquidated by the third party custodian agent and proceeds used to purchase the borrowed security which will be returned to the underlying principal lender. If the borrowed security cannot be purchased in the market, its equivalent value is returned to the underlying principal lender. Any excess value on the realization on the loan collateral ~~over the loan repayment obligation~~ will be returned by the third party custodian agent to the Dealer Member~~.~~;”

Comment #	Public comment	IIROC Staff response
	counterparty's right to collateral in the event of a default or Dealer Member insolvency. *[RBC Dominion Securities Inc. (RBC DS)]*	
17.	The proposal requires that where the written agency agreement does not include the additional terms, the margin required would be 100% of the market value. The proposed requirements would be overly cumbersome in comparison to the equivalent principal arrangement. In setting the margin requirements, IIROC should take into consideration that dealers may engage a financial institution as a counterparty as well as agent for different arrangements and therefore have a written principal agreement with the financial institution that contains the minimum terms under Note 5(a) ("minimum terms"); or that existing agency agreements may already contain the minimum terms and further coordination and negotiation must take place to ensure that such agreements reflect the proposed additional terms. Rather than requiring margin at 100% of the market value for such arrangements, we recommend that IIROC consider allowing a less punitive margin requirement for dealers that have existing written agreements containing the minimum terms. As written, the requirement for the addition of these terms would place an undue burden on Dealer Members to unnecessarily amend provisions in existing agreements, expose Dealer members to punitive capital requirements for not doing so and possibly have the unintended effect of limiting / eliminating the Dealer Member use of third party custodians as agents. Consequently, we ask that IIROC reconsider adding the	Please see our response to Comment #1.

Comment #	Public comment	IIROC Staff response
	requirement to include both of these additional terms in Agency Agreements. Notwithstanding our comments above, should Dealer Members be required to add any additional terms to existing agreements, we recommend that IIROC provide Dealer Members with a reasonable transition period to ensure proper negotiation and implementation of any new documentation requirements. *[RBC Dominion Securities Inc. (RBC DS)]*	
18.	**3. Classification of Sovereign Wealth Funds** As part of the Proposal, we urge IIROC to consider adding sovereign wealth funds as a specific type of entity that would fall under the definition of acceptable counterparty. By way of background, sovereign wealth funds are investment management entities funded by revenues, savings, budget surpluses, and / or reserves of sovereign nations and beneficially owned by the state. At this time, sovereign wealth funds do not directly qualify as one of the acceptable entities under the current definitions of AI or AC, such as foreign federal government or mutual funds. Hence Canadian dealers have been treating sovereign wealth funds as “Other” counterparties, though the credit risk associated such entities is comparable to an AI (foreign federal government of Basle Accord country) or an AC (foreign federal government of non-Basle accord country). Since arrangements with “Other” counterparties are subject to significantly higher capital treatment, we caution that the capital requirement has become	Regarding the inclusion of sovereign wealth funds in the AI and AC definitions, we believe those definitions are already general enough to qualify those funds if those sovereign wealth funds were guaranteed by their federal governments or have audited financial statements that could be assessed against the criteria in those definitions. Otherwise, it is very difficult to assess the counterparty credit risk of those funds.

Comment #	Public comment	IIROC Staff response
	a barrier for Canadian dealers to dealing with sovereign wealth funds, putting dealers at a disadvantage to global peers. *[RBC Dominion Securities Inc. (RBC DS)]*	

Discussion of four types of counterparties defined within IIROC's capital and margin rules

In order to more accurately assess the credit risk associated with dealing with individual and corporate clients, the IIROC capital and margin rules categorize each counterparty client with which a Dealer Member may transact as one of the following:

1. Acceptable institutions
2. Acceptable counterparties
3. Regulated entities
4. Other

Acceptable institutions

Acceptable institutions are considered the lowest credit risk clients. Dealer Members may transact with acceptable institutions on an unsecured basis provided that each transaction is confirmed within a reasonable period of time. The following clients qualify as acceptable institutions:

- Government of Canada, Bank of Canada and provincial governments and any related crown corporations and agencies;
- Foreign federal governments of signatory nations of the Basel Accord on banking and supervision;
- Canadian banks, Quebec savings banks, credit unions, caisses populaires, insurance companies, trust companies and loan companies licensed to do business in Canada or a province thereof with paid up capital and surplus in excess of $100 million;
- Foreign banks and trust companies subject to a satisfactory regulatory regime[1] with paid up capital and surplus in excess of $150 million;
- Canadian pension funds which are regulated either by the Office of Superintendent of Financial Institutions or a provincial pension commission, with total net assets in excess of $200 million; and
- Foreign pension funds subject to a satisfactory regulatory regime with total net assets on the in excess of $300 million.

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

Acceptable counterparties

Acceptable counterparties are considered to be clients of moderate credit risk. Dealer Members must, with some exceptions, transact with acceptable counterparties on a "value for value"[2] basis provided that each transaction is confirmed within a reasonable period of time. An exception is made for cash and security borrowing and lending transactions, as a modest amount of over-collateralization (i.e. 2% to 5%) is permitted in order in order to avoid requiring the dealer to post additional collateral during the term of the arrangement is response to minor market price fluctuations. The following clients qualify as acceptable counterparties:

- Canadian provincial capital cities and all other Canadian cities and municipalities, or their equivalents, with populations of 50,000 and over;
- Foreign federal governments which do not qualify as an "acceptable institution";
- Canadian banks, Quebec savings banks, credit unions, caisses populaires, insurance companies, trust companies and loan companies licensed to do business in Canada or a province thereof with paid up capital and surplus in excess of $10 million and less than or equal to $100 million;
- Foreign banks and trust companies subject to a satisfactory regulatory regime[3] with paid up capital and surplus in excess of $15 million and less than or equal to $150 million;
- Foreign insurance companies subject to a satisfactory regulatory regime with paid up capital and surplus in excess of $15 million;
- Canadian pension funds which are regulated either by the Office of Superintendent of Financial Institutions or a provincial pension commission, with total net assets in excess of $10 million and less than or equal to $200 million;
- Foreign pension funds subject to a satisfactory regulatory regime with total net assets on the in excess of $15 million and less than or equal to $300 million;
- Mutual funds subject to a satisfactory regulatory regime with total net assets in the fund in excess of $10 million;
- Corporations other than "regulated entities" with a minimum net worth of $75 million; and
- Trusts and limited partnerships with minimum total net assets in excess of $100 million.

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[2] Transactions performed on a "value for value" basis are those where the market value of the cash or securities received in by the investment dealer is equal to the market value of the cash or securities delivered out by the investment dealer.

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

Regulated entities

As is the case with acceptable counterparties, regulated entities are considered to be clients of moderate credit risk. Dealer Members must, with some exceptions, transact with regulated entities on a "value for value" basis provided that each transaction is confirmed within a reasonable period of time. To qualify as a regulated entity, the client must be a dealer and must be a member of the Canadian Investor Protection Fund or a member of a recognized exchange or association that:

- maintains or is a member of an investor protection regime equivalent to the Canadian Investor Protection Fund;
- requires the segregation by its members of customers' fully paid for securities;
- that has rules that set out specific methodologies for the segregation of, or reserve for, customer credit balances;
- that has established rules regarding Dealer Member and customer account margining;
- that 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
- that requires regular regulatory financial reporting by its members.

Examples of dealers that qualify as regulated entities include FINRA members, "full scope BIPR" investment firms regulated by the United Kingdom Financial Conduct Authority, firms with an Australian financial services licence regulated by the Australian Securities Exchange Limited and investment firms regulated by the Tokyo Stock Exchange, Inc.

Other

An "Other" counterparty is a client or dealer that does not qualify under any of the other counterparty categories. "Other" counterparties are considered to be clients of high credit risk. For this reason, no reliance is placed on the credit worthiness of the client/dealer and credit risk exposures may only be incurred with these clients in situations where the client has account security positions with regulatory "loan value"[4].

[4] The loan value of a security position is its market value less any margin required on the position to cover the risk of future loss.

Attachment F

Summary of margin impact of the revisions to the cash and securities borrowing and lending proposal

Ultimate securities borrow / lend agreement counterparty	Principal Agreement directly with ultimate counterparty	Principal Agreement where "Acceptable Institution" custodian is acting as a principal counterparty on behalf of ultimate counterparty	Agency Agreement (qualifying as equivalent to principal)			
			"Acceptable Institution" custodian is acting as an agent counterparty on behalf of ultimate counterparty	"Acceptable Counterparty" custodian is acting as an agent counterparty on behalf of ultimate counterparty	"Regulated Entity" custodian is acting as an agent counterparty on behalf of ultimate counterparty	"Other" counterparty custodian is acting as an agent counterparty on behalf of ultimate counterparty
Acceptable Institution	No margin is required where agreement is confirmed	No margin is required where agreement is confirmed	No margin is required where agreement is confirmed *[same as principal agreement with Acceptable Institution custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Acceptable Counterparty custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Regulated Entity custodian]*	Margin required is loan value deficiency amount *[same as principal agreement with Other counterparty custodian]*
Acceptable Counterparty	Margin required is excess overcollateralization amount	No margin is required where agreement is confirmed	No margin is required where agreement is confirmed *[same as principal agreement with Acceptable Institution custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Acceptable Counterparty custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Regulated Entity custodian]*	Margin required is loan value deficiency amount *[same as principal agreement with Other counterparty custodian]*
Regulated Entity	Margin required is excess overcollateralization amount	No margin is required where agreement is confirmed	No margin is required where agreement is confirmed *[same as principal agreement with Acceptable Institution custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Acceptable Counterparty custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Regulated Entity custodian]*	Margin required is loan value deficiency amount *[same as principal agreement with Other counterparty custodian]*
Other Counterparty	Margin required is loan value deficiency amount	No margin is required where agreement is confirmed	~~Margin~~No margin is required ~~is loan value deficiency amount~~where agreement is confirmed *[same as principal agreement with ~~Other counterparty~~Acceptable Institution custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Acceptable Counterparty custodian]*	Margin required is excess overcollateralization amount *[same as principal agreement with Regulated Entity custodian]*	Margin required is loan value deficiency amount *[same as principal agreement with Other counterparty custodian]*

Legend for colours used in the diagram above		Original Proposal's margin result (typical for custodian agent to be an Acceptable Institution)		Proposed Amendments' margin result for broadened scope to include a customer that is an Other counterparty (typical for custodian agent to be an Acceptable Institution)		Proposed Amendments' margin result for broadened scope (to proactively address non-typical situations where custodian agent could be one of the other counterparty types)