

## Chapter 13

# SROs, Marketplaces and Clearing Agencies

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### 13.3 Clearing Agencies

#### 13.3.1 CDS Clearing and Depository Services Inc. – Technical Amendments to CDS Procedures

##### CDS CLEARING AND DEPOSITORY SERVICES INC. (CDS®)

##### TECHNICAL AMENDMENTS TO CDS PROCEDURES

#### Participating in CDS Services:

- Chapter 15 – Collateral Administration – Section 15.1.2 - Delivering U.S. dollar cash as collateral (update)
- Chapter 16 – Collateral Pools – Section 16.6 – Special margin collateral pools (update) and section 16.6.1 - New York Link/DTC Direct Link special margin participant funds (new)

#### New York Link Participant Procedures:

- Chapter 6 – New York Link participant funds

#### DTC Direct Link Participant Procedures:

- Chapter 1 – About the DTC Direct Link Service – Section 1.3 – Net debit caps (update)
- Chapter 4 – DTC Direct Link participant funds (update)

### NOTICE OF EFFECTIVE DATE

#### A. DESCRIPTION OF THE CDS PROCEDURE AMENDMENTS

##### *Background*

CDS's New York Link (NYL) and DTC Direct Link (DDL) procedures were reviewed for accuracy and completeness by CDS staff. As a result of this review, the following two required amendments were identified relative to CDS's participant procedures.

##### **Special Margin Collateral**

Under certain conditions (e.g. if a participant is encountering financial difficulties), participants that subscribe to the NYL or DDL services may be asked to provide additional collateral (i.e. in addition to their NSCC participant fund for NYL, CDS participant fund for NYL and CDS participant fund for DDL requirements).

This additional (special) collateral is kept separate from the collateral related to the NSCC participant fund for NYL, CDS participant fund for NYL and CDS participant fund for DDL.

The NSCC special margin participant fund had been in place for the NSCC participant fund prior to the changes to the NYL and DDL services that went into effect on November 2, 2009, but it was not described in detail within CDS's external procedures.

This procedure amendment is intended to provide CDS participants with more detail relative to the NYL and DDL services related special margin participant funds.

##### **DTC Net Debit Caps**

On November 2, 2009 changes were made to the allocation of minimum and maximum DTC net debit caps to participants by CDS.

The amendments to the net debit cap procedure are designed to provide clarity relative to the minimum and maximum DTC net debit caps that are allocated by CDS to participants.

In the middle of September 2009, CDS provided the New York Link (NYL) and DTC Direct Link (DDL) participants with estimates of their CDS Participant Fund for New York Link and CDS Participant Fund for DTC Direct Link requirements that would be in effect for November 2, 2009.

When the NYL and DDL participants were first advised of what their participant fund requirements were expected to be on November 2, 2009, a number of them came back to CDS and asked if it would be possible to reduce the participant fund requirements.

CDS responded that reducing the maximum DTC net debit caps would be an option to consider in order to reduce their participant fund requirements and CDS subsequently provided the participants with revised participant fund requirements based on the proposed reduced DTC Net Debit Caps (NDCs). Participants had no concerns with reducing their NDCs since the optimization of amounts was based on actual activity and as the normal course of business participants with large DTC settlement activity have historically pre-funded their DTC settlements and it was clear that this would not have a material impact on their settlement activity.

CDS kept all NYL and DDL participants informed about the impact of lower NDCs on pre-funding and collateral requirements throughout the process and two CDS bulletins that contained information related to the changes to the DTC net debit caps were released on Oct 9 and Oct 30, 2009.

CDS decided to collateralize the maximum DTC net debit cap (NDC) for NYL and DDL similar to USD RCP. The maximum and minimum NDC amounts were determined based on the actual DTC settlement activity of sponsored participants. It was determined that participants with large settlement activity pre-fund their settlements at DTC despite having large NDC at DTC. Many smaller sized sponsored participants did not have enough DTC settlement activity to justify a minimum of \$10 million NDC that is allocated by DTC. It was determined that the largest NDC of \$20 million for NYL would provide be optimal in terms of leverage ratio and collateral requirements. It was also determined that the largest NDC of \$10 million for DDL would be optimal in terms of leverage ratio and collateral requirements.

CDS proactively worked with participants to come to optimal NDCs and the recommended cap was accepted by all participants with no concerns.

At the end of September 2009, CDS's Board of Directors approved CDS's recommendation to reduce the maximum DTC net debit cap to USD 20.0 million.

CDS then provided the New York Link (NYL) and DTC Direct Link (DDL) participants with revised estimates of their CDS Participant Fund for New York Link and CDS Participant Fund for DTC Direct Link requirements that would be in effect for November 2, 2009.

CDS reduced the maximum DTC net debit cap to US\$10.0 million for the DDL service, the minimum DTC net debit cap to US\$0.0 million from US\$10.0 million for the NYL & DDL services and the maximum DTC net debit cap for new NYL & DDL participants to US\$1.0 million from US\$10.0 million.

The reduction in the DTC net debit caps reduced the risk to CDS and reduced the participant fund requirements for the participants (i.e. the reduction in participant fund requirements more than offset the increase in pre-funding requirements). The lower NDCs also reduce CDS's payment and liquidity risk exposures at DTC. Since it was decided to collateralize largest NDCs in both NYL and DDL, lower NDCs reduce sponsored participants' collateral requirements.

#### *Description of Proposed Amendments*

The following amendments are proposed to CDS's external procedures:

Participating in CDS Services:

- Chapter 15 Collateral Administration – Section 15.1.2 – Delivering U.S. dollar cash as collateral – information related to the special margin collateral pools has been added
- Chapter 16 Collateral Pools – Section 16.6 – Special margin collateral pools – Text has been removed because the Montreal Exchange no longer advises CDS and because early warning does not just apply to Canadian dollar collateral pool members

- Chapter 16 Collateral Pools – Section 16.6.1 – New York Link/DTC Direct Link special margin participant funds – A table and text has been added relative to the NYL and DDL services special margin participant funds

New York Link Participant Procedures:

- Chapter 6 – New York Link participant funds – Text has been added related to the CDS participant fund for NYL – Special Margin and the NSCC participant fund for NYL – Special Margin

DTC Direct Link Participant Procedures:

- Chapter 1 – About the DTC Direct Link Service – Section 1.3 – Net debit caps - Text is being amended to more clearly reflect changes that were implemented to the allocation of DTC net debit caps by CDS on November 2, 2009
- Chapter 4 – DTC Direct Link participant funds - Text has been added related to the CDS participant fund for DDL – Special Margin

The CDS Procedures marked for the amendments may be accessed at the CDS website at:

<http://www.cds.ca/cdsclearinghome.nsf/Pages/-EN-blacklined?Open>.

CDS Procedure Amendments are reviewed and approved by CDS's Strategic Development Review Committee ("SDRC"). The SDRC determines or reviews, prioritizes and oversees CDS-related systems development and other changes proposed by participants and CDS. The SDRC's membership includes representatives from the CDS Participant community and it meets on a monthly basis.

These amendments were reviewed and approved by the SDRC on March 18, 2010.

#### **B. REASONS FOR TECHNICAL CLASSIFICATION**

The amendments proposed pursuant to this Notice are considered to be technical amendments as they pertain to matters of a technical nature in routine operating procedures and administrative practices relating to the settlement services.

Also, as stated within the external procedures, 'CDS reserves the right to increase or decrease the net debit cap at its discretion', as such the proposed amendments related to DTC net debit caps are considered to be technical as they simply add additional detail around the changes that were made by CDS in November, 2009.

#### **C. EFFECTIVE DATE OF THE CDS PROCEDURE AMENDMENT**

Pursuant to Appendix A ("Rule Protocol Regarding The Review And Approval Of CDS Rules By The OSC") of the Recognition and Designation Order, as amended on November 1, 2006, and Annexe A ("Protocole d'examen et d'approbation des Règles de Services de Dépôt et de Compensation CDS Inc. par l'Autorité des marchés financiers") of AMF Decision 2006-PDG-0180, made effective on November 1, 2006, CDS has determined that the proposed amendments will become effective on a date subsequently determined by CDS, and as stipulated in the related CDS Bulletin.

#### **D. QUESTIONS**

Questions regarding this notice may be directed to:

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