

Chapter 13

SRO Notices and Disciplinary Proceedings

13.1.1 CDS Notice and Request for Comments – Material Amendments to CDS Procedures Relating to CCP Collateral Requirements for Withdrawing Participant

CDS CLEARING AND DEPOSITORY SERVICES INC. (CDS)

MATERIAL AMENDMENTS TO CDS PROCEDURES

CCP COLLATERAL REQUIREMENTS FOR WITHDRAWING PARTICIPANT

REQUEST FOR COMMENTS

A. DESCRIPTION OF THE PROPOSED AMENDMENTS

The current Survivor Withdrawal option, as approved August 8th, 2006 by the Ontario Securities Commission (OSC), allows a CDS Participant to withdraw from a Central Counterparty (CCP) service in the event of a default by providing an additional five hundred percent (500%) of their current collateral requirement to the CCP service Participant Fund. The proposed amendment to CDS Procedures is intended to maintain a level of protection against a potential collateral shortfall comparable to the current level, taking into account recent changes to the collateral calculation for CCP services, by increasing the withdrawal collateral contribution for the Continuous Net Settlement (CNS) Service to seven hundred percent (700%) of a Participant's current collateral requirement. The current contribution level of 500% remains in effect, and unchanged, for the DetNet Service. The proposed amendment has been reviewed and approved by CDS' Risk Advisory Committee.

B. NATURE AND PURPOSE OF THE PROPOSED AMENDMENTS

The proposed amendment to the survivor withdrawal collateral requirement is requested subsequent to a recent change in the collateral calculation for the CNS CCP services. The change to the Mark-to-Market component of the collateral calculation (approved by the OSC on August 8th, 2006), resulted in an expected reduction in Participant collateral requirements of 35%. CDS has determined that requiring a withdrawing survivor to contribute 700% of their current collateral requirement to the CNS CCP service Participant Fund will provide protection against un-collateralized losses to the CNS Participant Fund that is comparable to the current level of protection against such an event. The withdrawal collateral requirement for DetNet remains unchanged.

C. IMPACT OF PROPOSED AMENDMENTS

The proposed amendment will increase the survivor withdrawal collateral requirement by 40%. This increased withdrawal collateral burden is effectively set-off against the reduction in CCP service collateral requirements. The increase is necessary in order to provide a high degree of certainty that the CNS CCP service Participant Fund will be able to cover un-collateralized losses. For instance, a situation may arise in which the default of a single Participant results in the withdrawal of all surviving members of the service. In such an event, losses would have to be covered by a) the collateral of the defaulting Participant, b) the collateral and withdrawal collateral of the surviving Participants, and c) available collateral. Testing by CDS' Risk Management department has determined that, at the reduced collateral levels resulting from the August, 2006 amendment to the collateral requirements calculation, a 500% withdrawal contribution would provide sufficient coverage for only 84% of all stress events. A 700% withdrawal contribution will provide such coverage for 93% of all stress events, and the protection is bolstered by the conservative assumptions inherent to the analysis.

D. DESCRIPTION OF THE PROCEDURE DRAFTING PROCESS

CDS is recognized as a clearing agency by the Ontario Securities Commission pursuant to Section 21.2 of the *Ontario Securities Act* and is authorized by the Autorité des marchés financiers to carry on business as a clearing agency pursuant to §§. 169 and 170 of the *Québec Securities Act*. In addition CDS is deemed to be the clearing house for CDSX, a clearing and settlement system designated by the Bank of Canada pursuant to Section 4 of the *Payment Clearing and Settlement Act*. The Ontario Securities Commission, the Autorité des marchés financiers and the Bank of Canada will hereafter be collectively referred to as the "Recognizing Regulators".

CDS Procedure Amendments originate from a number of sources, both internal and external, and may be standalone or consequential amendments. Standalone amendments are most often necessitated by internal systems changes or service enhancements, while consequential amendments stem from amendments to CDS Participant Rules and/or other regulatory requirements. CDS Procedure Amendments are reviewed and approved by CDS' Strategic Development Review Committee.

The amendments to Participant Procedures may become effective upon approval of the amendments by the Recognizing Regulators following public notice and comment.

E. IMPACT OF PROPOSED AMENDMENTS ON TECHNOLOGICAL SYSTEMS

CDS has determined that the proposed amendments will have no impact on its technological systems or those of its Participants.

F. COMPARISON TO OTHER CLEARING AGENCIES

Participants who use CDS services must be a member of a Fund established for that Function, and is a part of a Fund Credit Ring. Further, depending on a Participant's category, it must also be a member of a Category Credit Ring. In this way, the Risk of default within a Fund or Category Credit Ring is reduced. The unique structure of CDS' risk model, however, reduces the utility of a comparison to the risk mitigation strategies of other clearing agencies whose own risk model may differ significantly from CDS'.

G. PUBLIC INTEREST ASSESSMENT

In analyzing the impact of the proposed amendments to the Participant rules, CDS has determined that the implementation of these amendments would not be contrary to the public interest.

H. COMMENTS

Comments on the proposed amendments should be in writing and delivered by April 30, 2007 and delivered to:

Tony Hoffmann
Legal Counsel
The Canadian Depository for Securities Limited
85 Richmond Street West
Toronto, Ontario M5H 2C9

Fax: 416-365-1984
e-mail: attention@cds.ca

Copies should also be provided to the Autorité des marchés financiers and the Ontario Securities Commission by forwarding a copy to each of the following individuals:

M^e Anne-Marie Beaudoin
Directrice du secrétariat
Autorité des marchés financiers
Tour de la Bourse
800, square Victoria, C.P. 246, 22^e étage
Montréal (Québec) H4Z 1G3

Télécopieur : 514 864-6381
Courriel :
consultation-en-cours@lautorite.qc.ca

Cindy Petlock
Manager, Market Regulation
Capital Markets Branch
Ontario Securities Commission
Suite 1903, Box 55,
20 Queen Street West
Toronto, Ontario, M5H 3S8

Fax: 416-595-8940
e-mail: cpetlock@osc.gov.on.ca

CDS will make available to the public, upon request, copies of comments received during the comment period.

I. PROPOSED PROCEDURE AMENDMENTS

Appendix "A" contains text of current CDS Participant Procedure marked to reflect proposed amendments as well as text of these procedures reflecting the adoption of the proposed amendments.

J. QUESTIONS

Questions regarding this notice may be directed to:

Tony Hoffmann
Legal Counsel
The Canadian Depository for Securities Limited
85 Richmond Street West
Toronto, Ontario M5H 2C9

Fax: 416-365-1984
e-mail: attention@cds.ca

JAMIE ANDERSON
Managing Director, Legal

APPENDIX "A"
PROPOSED RULE AMENDMENT

Text of CDS Participant Rules marked to reflect proposed amendments	Text CDS Participant Rules reflecting the adoption of proposed amendments
<p>18.1 CCP survivor withdrawal</p> <p>The CCP survivor withdrawal option is a mechanism that enables participants in a central counterparty service to limit the loss allocation they are responsible for by withdrawing from the service when one or more members of the service defaults. This option is applicable only in the event of a default and does not affect the normal non-default withdrawal of a participant from a central counterparty service.</p> <p>The following rules and restrictions govern a survivor's withdrawal from a central counterparty service:</p> <ul style="list-style-type: none"> • A participant can only withdraw from a CCP service in which a member of that service has defaulted. • <u>On the day of withdrawal, a participant must pledge one of the following:</u> <ul style="list-style-type: none"> ○ A-If the participant must pledge is withdrawing from DetNet, then an additional 500 per cent of their DetNet collateral requirement in that CCP service to CDS on the day of withdrawal is required. ○ <u>If the participant is withdrawing from CNS, then an additional 700 per cent of their CNS collateral requirement is required.</u> <p>...</p>	<p>18.1 CCP survivor withdrawal</p> <p>The CCP survivor withdrawal option is a mechanism that enables participants in a central counterparty service to limit the loss allocation they are responsible for by withdrawing from the service when one or more members of the service defaults. This option is applicable only in the event of a default and does not affect the normal non-default withdrawal of a participant from a central counterparty service.</p> <p>The following rules and restrictions govern a survivor's withdrawal from a central counterparty service:</p> <ul style="list-style-type: none"> • A participant can only withdraw from a CCP service in which a member of that service has defaulted. • On the day of withdrawal, a participant must pledge one of the following: <ul style="list-style-type: none"> ○ If the participant is withdrawing from DetNet, then an additional 500 per cent of their DetNet collateral requirement is required. ○ If the participant is withdrawing from CNS, then an additional 700 per cent of their CNS collateral requirement is required. <p>...</p>