

## NOTICE AND REQUEST FOR COMMENT MATERIAL AMENDMENTS TO CDS EXTERNAL PROCEDURES

### Participant cash collateral interest rate rebate and negative interest charges

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

The Canadian Depository for Securities (“CDS”) is proposing amending its External Procedure Documents entitled “Participating in CDS Services” and “New York Link Participant Procedures” (collectively, the “External Procedures”) in order to clarify the existing provisions relating to interest rebate and interest charge on participants’ cash collateral deposits.

CDS proposes that the text *in blue* below be added in the External Procedures:

- **Participating in CDS Services - Section 15.1.3 - Interest Rebates / *Charges***

Participants with cash contributions in the CNS Participant Fund, CNS Default Fund, and Supplemental Liquidity Fund are eligible to receive interest on these funds on a semi-annual basis.

Interest is payable within 45 calendar days from the end of each semiannual period, ending March 31 and September 30, provided that the participants’ obligations to CDS have been fulfilled.

The interest rate is the rate earned by CDS in its current account on the first day of each month. The calculation of the interest payable *to the participants* is based on the participant’s pro-rata share of total cash on deposit, averaged over the six month period. *If a negative interest rate is charged to CDS, the negative interest will be passed through and charged back to the participant based on the participant’s pro-rata share of total cash on deposit, averaged over the six month period.*

- **New York Link Participant Procedures - Section 6.3 - CDS participant fund for New York Link (administered by CDS)**

New York Link participants must also contribute to a participant fund administered by CDS.

CDS calculates the participant fund requirement monthly.

All participant fund requirements may be satisfied in the form of eligible collateral. For more information, refer to Participating in CDS Services.

If a requested collateral contribution is not delivered by the specified deadline, the participant may be fined or suspended.

Cash is used to satisfy a CDS participant fund for New York Link contribution. For more information, see Delivering U.S. dollar cash as collateral in Participating in CDS Services.

#### **Making initial collateral contributions**

There is no minimum collateral contribution required from each participant.

#### **Making monthly collateral contributions**

Participants are notified of their collateral contribution requirements on a monthly basis. Collateral contribution requirements may be satisfied by delivering a collateral contribution to CDS in the form of eligible collateral and within the collateral limits.

All collateral contribution requirements must be delivered by 10:00 a.m. ET (8:00 a.m. MT, 7:00 a.m. PT) on the day it is due. If CDS does not receive the required collateral contribution by the specified deadline, the participant is fined. If the collateral contribution is still outstanding by 11:00 a.m. ET (9:00 a.m. MT, 8:00 a.m. PT), the participant is suspended.

Participant cash contributions to the CDS participant fund for New York Link are eligible to earn interest. *The calculation of the interest payable to the participants is based on the participant's pro-rata share of total cash on deposit, averaged over the six month period. If a negative interest rate is charged to CDS, the negative interest will be passed through and charged back to the participant based on the participant's pro-rata share of total cash on deposit, averaged over the six month period.*

The proposed amendments are also provided in Appendix “A” to this Notice.

## **B. NATURE AND PURPOSE OF THE PROPOSED CDS PROCEDURE AMENDMENTS**

CDS is proposing to modify the “Interest Rebates” section of its External Procedures, in order to clarify that, to the extent CDS is being charged any negative interest on its CAD accounts and USD accounts where the cash contributions to the CNS Participant Fund, the CNS Default Fund, the Supplemental Liquidity Fund and CDS Participant Fund for New York Link are deposited, such negative interest will be considered a charge that will be passed through to the participants.

The interest rate earned by CDS on cash collateral is distributed to participants based on their pro-rata share of total cash on deposit. To date CDS has not had a situation where interest rates have been negative. However, with the recent Covid-19 pandemic circumstances, and the impact of such pandemic on the volatility of the Canadian and American financial markets, CDS recognizes that there is a possibility of negative interest rates being charged to CDS by its banks (including Bank of Canada and any US commercial bank holding USD cash collateral contributions) in the future.

In the event CDS must charge back any negative interests to the participants, CDS will promptly communicate the information via the Bulletin process to ensure timely communication of the situation to all participants.

## **C. IMPACT OF THE PROPOSED CDS PROCEDURE AMENDMENTS**

In the event a negative interest rate is charged to CDS by its banks (including Bank of Canada and any US commercial bank holding USD cash collateral contributions), CDS would pass through this charge to the participant.

### **C.1 Competition**

The proposed amendments to the External Procedures will apply to all CDS Participants with cash contributions in the CNS Participant Fund, CNS Default Fund, Supplemental Liquidity Fund and CDS Participant Fund for New York Link. If CDS is committed to distributing to the Participants the net amount of any interests received by CDS from its banks on the invested collateral of the Participants, the Participants must logically bear the risk of being charged any negative interests.

### **C.2 Risks and Compliance Costs**

The proposed External Procedures amendments are intended to clarify interest fluctuations due to market volatility. Some CDS Participants may see some impacts of the negative interest rate charge. However, as stated in the CDS Rules, this burden may be partially offset since CDS Participants generally receive

the net amount of any interest, dividend or income received by CDS on the invested collateral of the Participants, in accordance with the details included in the External Procedures, provided the Participant's obligations to CDS have been fulfilled.

**C.3 Comparison to International Standards – (a) Committee on Payment and Settlement Systems of the Bank for International Settlements, (b) Technical Committee of the International Organization of Securities Commissions, and (c) the Group of Thirty**

The proposed amendments to the External Procedures are entirely consistent with all relevant international standards. These amendments are intended to support CDS' observance that due to market volatility there is a possibility of negative interest rates being charged to CDS by its banks.

**D. DESCRIPTION OF THE PROCEDURE DRAFTING PROCESS**

**D.1 Development Context**

CDS legal, risk management and operations representatives have prepared documents describing the proposed amendments to External Procedures.

**D.2 Procedure Drafting Process**

The proposed amendments were drafted by representatives of CDS Operations Team and the Risk Management team, in consultation with CDS Legal team.

CDS procedure amendments were reviewed and approved by CDS's strategic development review committee (SDRC) on June 25, 2020. 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.

**D.3 Issues Considered**

In drafting the amendments to the External Procedures, CDS' primary consideration was to clarify that, in the event a negative interest rate is charged to CDS, this negative interest will be passed through and charged back to the participant.

**D.4 Consultation**

Users responsible for providing comments/updates to the External Procedures were consulted to ensure effective implementation. The proposed procedure amendments were presented to the SDRC on June 25, 2020. The project office managed the various work streams deliverables including Operational process, Risk models/measurements, various Committees, external procedures and rule changes, to be presented for Board approval (when applicable) and for Public Comment.

**D.5 Alternatives Considered**

In considering the proposed External Procedures amendments, CDS determined that the pass through charge was consistent with interest earned by CDS, and interest payment is distributed based on the participant's pro-rata share of total cash on deposit. The negative interest will then be charged back in the same manner.

**D.6 Implementation Plan**

CDS is recognized as a clearing agency by the Ontario Securities Commission pursuant to section 21.2 of the Securities Act (Ontario), by the British Columbia Securities Commission pursuant to Section 24(d) of

the Securities Act (British Columbia) and by the Autorité des marchés financiers (“AMF”) pursuant to section 169 of the Securities Act (Québec). 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 British Columbia Securities Commission, the Autorité des marchés financiers and the Bank of Canada will hereafter be collectively referred to as the “Recognizing Regulators”. The amendments to CDS Participant External Procedures are expected to become effective on a date to be determined by CDS (such date expected to be in **Q3 2020**), such date to fall subsequent to approval of the amendments by the Recognizing Regulators following public notice and comment and be contingent on completion of appropriate testing and applicable notice to CDS participants.

## **E. TECHNOLOGICAL SYSTEMS CHANGES**

The proposed amendments to the External Procedures are not expected to have an impact on technological systems, or require changes to such systems for CDS, CDS participants, or other market participants.

## **F. COMPARISON TO OTHER CLEARING AGENCIES**

Given the nature of the proposed amendments, CDS is of the view that a comparative analysis with other clearinghouses is not required. However, CDS notes that Canadian Derivative Clearing Corporation (CDCC) references negative interest rates in its Operations Manual.

In addition to the foregoing, CDS notes that a few other clearing counterparties have included the notion of negative interests into their rules or procedures:

### **Eurex Clearing 3.4.4**

*“Eurex Clearing AG may determine from time to time to either pay interest **or charge negative interest** on Eligible Margin Assets in the form of cash actually delivered by a Clearing Member or a Basic Clearing Member (or Clearing Agent acting for the account of the Basic Clearing Member) to Eurex Clearing AG in respect of Margin. Eurex Clearing AG publishes information on the calculation of interest rates or **negative interest rates** as well as any changes to the applicable calculation method due to extraordinary market conditions or market disruptions on its website ([www.eurexclearing.com](http://www.eurexclearing.com)). Such information will be amended from time to time and published accordingly. **When determining to charge negative interest**, Eurex Clearing AG shall consider the currently applicable benchmark interest rates and interest rates charged by the central banks or commercial banks. Any income on Eligible Margin Assets in form of Securities actually delivered by a Clearing Member or a Basic Clearing Member to Eurex Clearing AG in respect of Margin shall be subject to the specific provisions of the Elementary Clearing Model Provisions, the ISA Provisions or the Basic Clearing Member Provisions”*

### **LCH Limited - Section 10 (f)**

*“Interest calculated on a basis determined from time to time by the Clearing House in accordance with the Procedures may at the Clearing House’s discretion (but subject to the provisions of the Default Rules and to Regulation 66(d) be paid, or, in **the case of negative interest rates, be charged**, on amounts standing to the credit of any of the Member’s Proprietary Accounts and/or Client Accounts.”*

### **LCH.Cleernet LLC - Regulation 306**

*“Interest shall accrue on an amount equal to the Clearing House’s contingent obligation to repay a Clearing Member’s Contribution from the time such Contributions are paid until such time that they are repaid to the Clearing Member or until such time that they (or any portion thereof) are applied or offset under Regulation 308, Regulation 310 or as otherwise provided under the Rulebook, in such manner as provided by the Procedures, and at a rate of interest linked to the Fed Funds Rate published on a*

*particular day (or, in relation to any day for which a Fed Funds Rate is not available, the Fed Funds Rate most recently published before such day), but determined by the Clearing House in its sole discretion in light of market conditions at each applicable time by the Clearing House, and notified by the Clearing House to the Clearing Members. **In the event that the Fed Funds Rate is negative, interest shall be payable by the Clearing Members to the Clearing House.***

## G. PUBLIC INTEREST ASSESSMENT

CDS has determined that the proposed amendments are not contrary to the public interest.

## H. COMMENTS

Comments on the proposed amendments should be in writing and submitted within 30 calendar days following the date of publication of this notice in the Ontario Securities Commission Bulletin to:

Anne Fiddes, VP Integrated Operations  
Telephone: 416-285-1031  
Email: [CDSrelationshipmgmt@tmx.com](mailto:CDSrelationshipmgmt@tmx.com)

Relationship Management  
Email: [CDSrelationshipmgmt@tmx.com](mailto:CDSrelationshipmgmt@tmx.com)

CDS Clearing and Depository Services Inc.  
100 Adelaide Street West  
Toronto, Ontario  
M5H 1S3

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:

Philippe Lebel  
Corporate Secretary and  
Executive Director, Legal Affairs  
Autorité des marchés financiers  
Place de la Cité, tour Cominar  
2640 Laurier boulevard, suite 400  
Québec (Québec) G1V 5C1

Télécopieur: (514) 864-8381  
Courrier électronique:  
[consultation-en-cours@lautorite.qc.ca](mailto:consultation-en-cours@lautorite.qc.ca)

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  
email: [marketregulation@osc.gov.on.ca](mailto:marketregulation@osc.gov.on.ca)

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

## Canadian dollar cash withdrawals

If a request for a cash withdrawal is received by 10 a.m. ET:

- Amounts less than or equal to \$10 million may be withdrawn after 10 a.m. ET on the next business day following the withdrawal request<sup>1</sup>
- Amounts greater than \$10 million may be withdrawn after 10 a.m. ET two business days following the withdrawal request

### 15.1.2 Delivering U.S. dollar cash as collateral

To deposit U.S. dollar cash as collateral for USD collateral pools and/or participant funds other than the CDS participant fund for New York Link, initiate a Fedwire payment to the following CDS account.

Bank	Harris National Association
Telegraphic ID	HARRIS CHGO
Account number	203-212-6
ABA number	071000288
FAO	CDS Clearing and Depository Services Inc. (include the Participant Fund ID)

To deposit U.S. dollar cash as collateral for the CDS participant fund for New York Link, initiate a Fedwire payment to the following CDS account.

Bank	Wells Fargo Bank, N.A.
SWIFT code	WFBIUS6S
Account number	4597225077
ABA number	121000248
FAO	CDS Clearing and Depository Services Inc. (include the Participant Fund ID)

CDS monitors the accounts to ensure that the funds are deposited to CDS's account. CDS then enters the cash value received in the Collateral Management System.

### 15.1.3 Interest rebates and charges

Participants with cash contributions in the CNS Participant Fund, CNS Default Fund and Supplemental Liquidity Fund are eligible to receive interest on these funds on a semi-annual basis.

---

<sup>1</sup> Cash collateral withdrawals may be subject to CDS's own banking restrictions. CDS will confirm by 10:30 a.m. ET to any participant with a withdrawal request if that request cannot be fulfilled by the next business day following the withdrawal request.

Interest is payable within 45 calendar days from the end of each semi-annual period, ending March 31 and September 30, provided that the participants' obligations to CDS have been fulfilled.

The interest rate is the rate earned by CDS in its current account on the first day of each month. The calculation of the interest payable to the participants is based on the participant's pro rata share of total cash on deposit, averaged over the six month period. If a negative interest rate is charged to CDS, the negative interest will be passed through and charged back to the participant based on the participant's pro-rata share of total cash on deposit, averaged over the six month period.

#### 15.1.4 Making collateral contributions

Securities used as collateral are pledged using the Pledge to CDS Menu function from the participant's ledgers (non-risk account) to the CAL assigned for that pool, funds or Supplemental Liquidity Fund. Pledges are confirmed only if all the required edits are satisfied. Settlement of the pledge moves the securities into the CAL and the securities are then managed by CDS in its role as the administrator.

Participants may substitute other securities into their CAL and release the original contribution back to their ledgers. A participant must maintain sufficient value of securities in their CAL at all times.

The calculations required for given activities are made on an individual security basis. When collateral administrators calculate their collateral contributions, the calculation must use the current market price, a margin discount factor and an accrued interest calculation, if any, for each security contributed. The applicable value of a security that is contributed as collateral is calculated as follows:

$$\text{Applicable value} = \text{Market value} - (\text{Market value} \times \text{Margin}) + \text{Accrued interest}$$

Each collateral administrator is responsible for ensuring that the applicable value of their collateral contributions meets or exceeds their required contribution.

### **Making initial collateral contributions**

There is no minimum collateral contribution required from each participant.

### **Making monthly collateral contributions**

Participants are notified of their collateral contribution requirements on a monthly basis. Collateral contribution requirements may be satisfied by delivering a collateral contribution to CDS in the form of eligible collateral and within the collateral limits.

All collateral contribution requirements must be delivered by 10:00 a.m. ET (8:00 a.m. MT, 7:00 a.m. PT) on the day it is due. If CDS does not receive the required collateral contribution by the specified deadline, the participant is fined. If the collateral contribution is still outstanding by 11:00 a.m. ET (9:00 a.m. MT, 8:00 a.m. PT), the participant is suspended.

Participant cash contributions to the CDS participant fund for New York Link are eligible to earn interest. The calculation of the interest payable to the participants is based on the participant's pro-rata share of total cash on deposit, averaged over the six month period. If a negative interest rate is charged to CDS, the negative interest will be passed through and charged back to the participant based on the participant's pro-rata share of total cash on deposit, averaged over the six month period.

#### **6.3.1 DTC and NSCC settlements components**

The CDS participant fund for New York Link is made up of the following components:

- [DTC settlements component](#) on page 31
- [NSCC settlements component](#) on page 32.

#### **DTC settlements component**

The DTC settlements component of the CDS participant fund for New York Link covers the risk of default for the New York Link participant with the largest payment obligation to DTC. In a default situation, CDS must pay DTC the amount owed by the New York Link participant by the end-of-day.

## Canadian dollar cash withdrawals

If a request for a cash withdrawal is received by 10 a.m. ET:

- Amounts less than or equal to \$10 million may be withdrawn after 10 a.m. ET on the next business day following the withdrawal request<sup>1</sup>
- Amounts greater than \$10 million may be withdrawn after 10 a.m. ET two business days following the withdrawal request

### 15.1.2 Delivering U.S. dollar cash as collateral

To deposit U.S. dollar cash as collateral for USD collateral pools and/or participant funds other than the CDS participant fund for New York Link, initiate a Fedwire payment to the following CDS account.

Bank	Harris National Association
Telegraphic ID	HARRIS CHGO
Account number	203-212-6
ABA number	071000288
FAO	CDS Clearing and Depository Services Inc. (include the Participant Fund ID)

To deposit U.S. dollar cash as collateral for the CDS participant fund for New York Link, initiate a Fedwire payment to the following CDS account.

Bank	Wells Fargo Bank, N.A.
SWIFT code	WFBIUS6S
Account number	4597225077
ABA number	121000248
FAO	CDS Clearing and Depository Services Inc. (include the Participant Fund ID)

CDS monitors the accounts to ensure that the funds are deposited to CDS's account. CDS then enters the cash value received in the Collateral Management System.

### 15.1.3 Interest rebates and charges

Participants with cash contributions in the CNS Participant Fund, CNS Default Fund and Supplemental Liquidity Fund are eligible to receive interest on these funds on a semi-annual basis.

---

<sup>1</sup> Cash collateral withdrawals may be subject to CDS's own banking restrictions. CDS will confirm by 10:30 a.m. ET to any participant with a withdrawal request if that request cannot be fulfilled by the next business day following the withdrawal request.

Interest is payable within 45 calendar days from the end of each semi-annual period, ending March 31 and September 30, provided that the participants' obligations to CDS have been fulfilled.

The interest rate is the rate earned by CDS in its current account on the first day of each month. The calculation of the interest payable to the participants is based on the participant's pro rata share of total cash on deposit, averaged over the six month period. If a negative interest rate is charged to CDS, the negative interest will be passed through and charged back to the participant based on the participant's pro-rata share of total cash on deposit, averaged over the six month period.

#### **15.1.4 Making collateral contributions**

Securities used as collateral are pledged using the Pledge to CDS Menu function from the participant's ledgers (non-risk account) to the CAL assigned for that pool, funds or Supplemental Liquidity Fund. Pledges are confirmed only if all the required edits are satisfied. Settlement of the pledge moves the securities into the CAL and the securities are then managed by CDS in its role as the administrator.

Participants may substitute other securities into their CAL and release the original contribution back to their ledgers. A participant must maintain sufficient value of securities in their CAL at all times.

The calculations required for given activities are made on an individual security basis. When collateral administrators calculate their collateral contributions, the calculation must use the current market price, a margin discount factor and an accrued interest calculation, if any, for each security contributed. The applicable value of a security that is contributed as collateral is calculated as follows:

$$\text{Applicable value} = \text{Market value} - (\text{Market value} \times \text{Margin}) + \text{Accrued interest}$$

Each collateral administrator is responsible for ensuring that the applicable value of their collateral contributions meets or exceeds their required contribution.

### **Making initial collateral contributions**

There is no minimum collateral contribution required from each participant.

### **Making monthly collateral contributions**

Participants are notified of their collateral contribution requirements on a monthly basis. Collateral contribution requirements may be satisfied by delivering a collateral contribution to CDS in the form of eligible collateral and within the collateral limits.

All collateral contribution requirements must be delivered by 10:00 a.m. ET (8:00 a.m. MT, 7:00 a.m. PT) on the day it is due. If CDS does not receive the required collateral contribution by the specified deadline, the participant is fined. If the collateral contribution is still outstanding by 11:00 a.m. ET (9:00 a.m. MT, 8:00 a.m. PT), the participant is suspended.

Participant cash contributions to the CDS participant fund for New York Link are eligible to earn interest. The calculation of the interest payable to the participants is based on the participant's pro-rata share of total cash on deposit, averaged over the six month period. If a negative interest rate is charged to CDS, the negative interest will be passed through and charged back to the participant based on the participant's pro-rata share of total cash on deposit, averaged over the six month period.

#### **6.3.1 DTC and NSCC settlements components**

The CDS participant fund for New York Link is made up of the following components:

- [DTC settlements component](#) on page 31
- [NSCC settlements component](#) on page 32.

#### **DTC settlements component**

The DTC settlements component of the CDS participant fund for New York Link covers the risk of default for the New York Link participant with the largest payment obligation to DTC. In a default situation, CDS must pay DTC the amount owed by the New York Link participant by the end-of-day.