

Chapter 5

Rules and Policies

5.1.1 OSC Rule 14-502 (Commodity Futures Act) Designation of Additional Commodities and Companion Policy 14-502CP

ONTARIO SECURITIES COMMISSION RULE 14-502 (COMMODITY FUTURES ACT) DESIGNATION OF ADDITIONAL COMMODITIES

PART 1 – DESIGNATION OF ADDITIONAL COMMODITIES

1.1 Designation of Additional Commodities - In addition to the commodities listed in section 1 of the Commodity Futures Act, each of the following is designated as a commodity:

- (a) Energy and fuel, including gas, oil, electricity and energy-related products whether in their original or processed state, and any by-products thereof;
- (b) Weather, including temperatures, precipitation levels, hours of sunshine, or humidity, or any other natural occurrence;
- (c) A product based on environmental quality, including emissions or emission credits;
- (d) Water;
- (e) An interest rate;
- (f) A credit or mortgage obligation;
- (g) A security as the term is defined under the *Securities Act*, except for a security described in paragraph (p) of the definition;
- (h) An index, economic indicator, series or any other numeric reference;
- (i) The occurrence of an identified specific future act or event; or
- (j) Any interest that is a value determined with reference to any commodity, good, article, service, right or interest, or the relationship between any such values, or any combination thereof.

PART 2 - EFFECTIVE DATE

2.1 Effective Date - This Rule comes into effect on May 16, 2005.

**COMPANION POLICY 14-502CP (COMMODITY FUTURES ACT)
DESIGNATION OF ADDITIONAL COMMODITIES**

PART 1 PURPOSE OF THE COMPANION POLICY

1.1 Purpose - The purpose of this companion policy is to state the views of the Commission on various matters related to OSC Rule 14-502 (Commodity Futures Act) Designation of Additional Commodities (Rule), including

- (a) a discussion of the rationale for the Commission implementing the Rule, the general approach taken and the regulatory purpose of the Rule, and
- (b) providing more detail and interpretation of various terms and provisions of the Rule.

PART 2 PURPOSE OF THE RULE

2.1 Purpose of the Rule - Commodity derivatives markets have evolved from their historical agricultural roots to offer products based on a wide ranging and diverse set of underlyers. The designation of commodities in the Rule and the revocation of section 2 of the Regulation (Regulation) made under the *Commodity Futures Act* (Ontario) (CFA) is designed to take these market developments into account and provide the Commission with the ability to deal with them in a timely and efficient manner.

PART 3 COMMODITIES

3.1 Discussion of Designated Commodities - The following paragraphs describe the items that are designated as commodities in the Rule. Some of the designated items are new and others are clarifications and revisions to matters that were included in section 2 of the Regulation that was revoked when the Rule came into effect. The Commission believes that contracts based on these commodities should be regulated under the CFA in a manner that is consistent with the approach to products based on commodities currently captured by the definition. In addition, the regulation of these products will protect the integrity of capital markets, especially the futures markets and their participants, and ensure the Commission pursues an approach that is in keeping with a large number of other jurisdictions that regulate such products.

- (a) *Energy and fuel, including gas, oil, electricity and energy-related products whether in their original or processed state, and any by-products thereof*

Since the deregulation of energy markets, a number of exchanges have been established to trade a wide range of energy-based derivative products.

This paragraph includes, but is not limited to, wind, solar and tidal power, energy produced from household or industrial waste, and energy produced from nuclear, coal, wood, oil, gas, hydro-electric and sustainable fuel sources.

- (b) *Weather, including temperatures, precipitation levels, hours of sunshine, or humidity, or any other natural occurrence*

Weather derivatives have evolved over recent years from bilaterally negotiated, over-the-counter (OTC) transactions into more standardized products. As a result weather-based products are being listed on foreign exchanges.

- (c) *A product based on environmental quality, including emissions or emission credits*

The OTC market in emission credits has evolved with contracts becoming more standardized. Although environment-based products are not currently actively traded on exchange platforms, the Commission has designated products based on environmental quality as commodities in anticipation of their migration to on-exchange trading.

This paragraph includes, but is not limited to, emission credits and other industrial emission-based products.

- (d) *Water*

Water is being designated as a commodity in anticipation of the trading of futures contracts based on water quality or water supply.

This paragraph includes, but is not limited to, water sanitation and filtration and the supply of drinking water.

e) *An interest rate*

Interest rates include, but are not limited to, central bank interest rates and commercial interest rates, including benchmark interest rates such as Bankers Acceptances, Eurodollar and Libor.

f) *A credit or mortgage obligation*

Securitisation of credit receivables is now common practice in financial markets with the products upon which these receivables are based becoming increasingly standardized. The Commission has designated these obligations as commodities in anticipation of futures contracts being based upon them.

This includes, but is not limited to, mortgages, credit card receivables and car loans.

g) *A security as the term is defined under the Securities Act, except for a security described in paragraph (p) of the definition*

This includes, but is not limited to, all securities including equities, bonds, warrants or options on securities. This also clarifies that single stock futures are regulated under the CFA.

h) *An index, economic indicator, series or any other numeric reference*

The trading of both narrow- and broad-based equity indices has become increasingly popular over recent years. The expansion to include economic indicators and other references is designed to take into account products based on economic data and other benchmarks used in derivative transactions.

This paragraph includes, but is not limited to, narrow- and broad-based indices, inflation rates, consumer prices and job data.

i) *The occurrence of an identified specific future act or event*

Event-based derivatives are becoming increasingly common with a number of niche exchanges offering futures products based on specific events such as election results and credit defaults.

This includes, but is not limited to, credit default obligations.

j) *Any interest that is a value determined with reference to any commodity, good, article, service, right or interest, or the relationship between any such values, or any combination thereof*

Many contracts that are now traded do not involve the physical delivery of the commodity and are often cash settled in lieu of physical delivery. Commodities include both an underlying interest that is a commodity and an interest that is a value, interest or right relating to a physical commodity, or any combination of or relationship between commodities.

This includes, but is not limited to, a cash settled futures contract and contracts for differences.