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	<input type="checkbox"/> MCEX

**CIRCULAR**  
**April 1<sup>st</sup>, 2010**

**REQUEST FOR COMMENTS**

**TEN-YEAR GOVERNMENT OF CANADA BOND FUTURES (CGB):  
MODIFICATION OF THE THRESHOLD LEVEL FOR BLOCK TRADES**

**AMENDMENTS TO PROCEDURES APPLICABLE TO THE EXECUTION OF BLOCK  
TRADES**

The Rules and Policies Committee of Bourse de Montréal Inc. (the Bourse) has approved amendments to the Procedures applicable to the execution of block trades (Procedures) of the Bourse in order to lower the CGB block trade threshold level from 2,000 to 1,500. The Bourse intends to lower the threshold level in the month of May 2010.

Comments on the implementation of the proposed additions must be submitted within 30 days following the date of publication of the present, at the latest on **April 30<sup>th</sup>, 2010**. Please submit your comments to:

*Mr. François Gilbert*  
*Vice-President, Legal Affairs, Derivatives*  
*Bourse de Montréal Inc.*  
*Tour de la Bourse*  
*P.O. Box 61, 800 Victoria Square*  
*Montréal, Quebec H4Z 1A9*  
*E-mail: legal@m-x.ca*

Circular no.: 034-2010

A copy of these comments shall also be forwarded to the Autorité des marchés financiers (the Autorité) to:

*Ms. Anne-Marie Beaudoin  
Director – Secretariat of L'Autorité  
Autorité des marchés financiers  
800 Victoria Square, 22<sup>nd</sup> Floor  
P.O. Box 246, Tour de la Bourse  
Montréal (Quebec) H4Z 1G3  
E-mail: [consultation-en-cours@lautorite.qc.ca](mailto:consultation-en-cours@lautorite.qc.ca)*

## **Appendices**

For your information, you will find in appendices an analysis document of the proposed amendments as well as the amended procedures. The implementation date of the proposed amendments will be determined by the Bourse, in accordance with the self-certification process as determined by the Derivatives Act (R.S.Q., chapter I-14.01).

## **Process for Changes to the Rules**

The Bourse is authorized to carry on business as an exchange and is recognized as a self-regulatory organization (SRO) by the Autorité. The Board of Directors of the Bourse has delegated to the Rules and Policies Committee of the Bourse its powers to approve and amend the Rules and Procedures. The Rules of the Bourse are submitted to the Autorité in accordance to the self-certification process as determined by the Derivatives Act (R.S.Q., chapter I-14.01).

In its SRO capacity, the Bourse assumes market regulation and supervision responsibilities of its approved participants. The responsibility for regulating the market and the approved participants of the Bourse comes under the Regulatory Division of the Bourse (the Division). The Division carries on its activities as a distinct business unit separate from the other activities of the Bourse.

The Division is under the authority of a Special Committee appointed by the Board of Directors of the Bourse. The Special Committee is empowered to recommend to the Board of Directors the approval or amendment of some aspects of the Rules of the Bourse governing approved participants, among which, the Rules relating to margin and capital requirements. The Board of Directors has delegated to the Rules and Policies Committee of the Bourse its powers to approve or amend these Rules with recommendation from the Special Committee. These changes are submitted to the Autorité for approval.



**TEN-YEAR GOVERNMENT OF CANADA BOND FUTURES (CGB):  
MODIFICATION OF THE THRESHOLD LEVEL FOR BLOCK TRADES**

**AMENDMENTS TO PROCEDURES OF BOURSE DE MONTRÉAL INC. APPLICABLE  
TO THE EXECUTION OF BLOCK TRADES**

Since the beginning of the credit crunch (July 2007), there has been a sharp drop in the volume of exchange-traded interest rate derivatives as market participants have been adversely impacted by de-leveraging and credit limitation issues. Consequently, market participants have significantly reduced their exposure to interest rate derivatives products. Since April 2009, the low interest rate environment has further depressed the volume of interest rate derivatives.

In-line with the sharply lower trading volumes on global derivatives exchanges, the volume of interest rate derivatives products at the Montreal Exchange has declined sharply as well.

Consequently, the Bourse is suggesting that the threshold level for block trades executed on the CGB be lowered. Block trade volume was robust prior to the start of the credit crisis representing 7% of the CGB's monthly volume. Since the threshold level for block trades in the CGB was increased from 1,500 to 2,000, the trend in the volume of the CGB has consistently declined – in step with a decline in the proportion of CGB block trades as well. In November 2009, block trade volume represented only 1% of the total volume of the CGB. The graph in the Appendix (section VIII) illustrates the decline in the monthly volume of the CGB futures contract and the decline in the proportion of block trades.

**I. OVERVIEW**

**a) Proposed Procedures Amendments**

It is proposed to amend the procedures applicable to the execution of block trades of the Bourse in order to lower the CGB block trade threshold level from 2,000 to 1,500. The Bourse proposes this amendment so that the new threshold level more accurately reflects the current market conditions of low volume in the CGB.

**II. RATIONALE**

- The block trade threshold level for the CGB contract was increased from 1,500 to 2,000 contracts in July 2007. The change in the block trade threshold level coincided with the start of the credit crunch in July 2007, which coincided as well with a

considerable decline in the volume of interest rate derivatives products across the globe, including the CGB contracts listed at the Montréal Exchange.

- For the periods of July 2007 to June 2008 and July 2008 to June 2009, an analysis on block trades shows that block trades have an impact on the market price and volume since the threshold level is too high compared to the low volume of activity in the CGB. In fact, in approximately 90% of block trades analyzed, the market cannot absorb the size of the block without provoking the following market disturbances: the block trade price falling outside the bid-ask prices and/or an increase of volume activity around the time the block trade is executed/reported).
- To determine the threshold level, we propose an analysis, whose methodology and results are explained in the Appendix (section VIII). The results for the first 10 months of 2009 show that an average transaction size of 1,513 contracts significantly disrupts the CGB market price and/or volume. The study suggests that by setting the block trade threshold level at 1,500 contracts (a survey of market participant confirms a threshold level at 1,500), the new threshold level will more accurately reflect the current market conditions of low volume in the CGB contracts.
- CGB open interest reached a critical level in July 2009, coming close to the 100,000 mark. Although the CGB open interest has rebounded to 158,000 contracts in November 2009, the CGB contract remains historically low. The block trade facility is not readily accessible to all market participants since the threshold level is too high given the current dynamics of the CGB market (with low volume and small transaction sizes of about 3 contracts on average). By lowering the threshold level, the block trade facility will be more accessible to market participants, enhancing the liquidity and open interest of the CGB contract.

### **III. SUMMARY OF THE PROPOSED AMENDMENTS TO THE PROCEDURES OF THE BOURSE**

#### **Procedures applicable to the execution of block trades**

The Bourse proposes to amend the procedures applicable to the execution of block trades, to lower the CGB block trades threshold from 2,000 to 1,500.

Due to the rapid change in the market environment, the Bourse proposes to review the block trades threshold on a yearly basis. The review will be based on the criteria proposed by the AMF to assess the impact of block trades on the CGB price. The Bourse will also ensure that the block trades will not represent more than 10% of the total CGB volume.

### **IV. OBJECTIVE OF THE PROPOSED AMENDMENTS TO THE PROCEDURES OF THE BOURSE**

The objective of the proposed amendments to procedures applicable to the execution of block trades is to lower the CGB block trades threshold from 2,000 to 1,500 in order to accurately reflect the current market conditions of low volume in the CGB contracts.

### **V. PUBLIC INTEREST**

The amendments to the Procedures applicable to the execution of block trades are proposed in order to make the use of the CGB contract more efficient for market participants who have expressed their support to lower the block trades threshold for the purpose of improving their trading and/or risk management strategies.

## **VI. PROCESS**

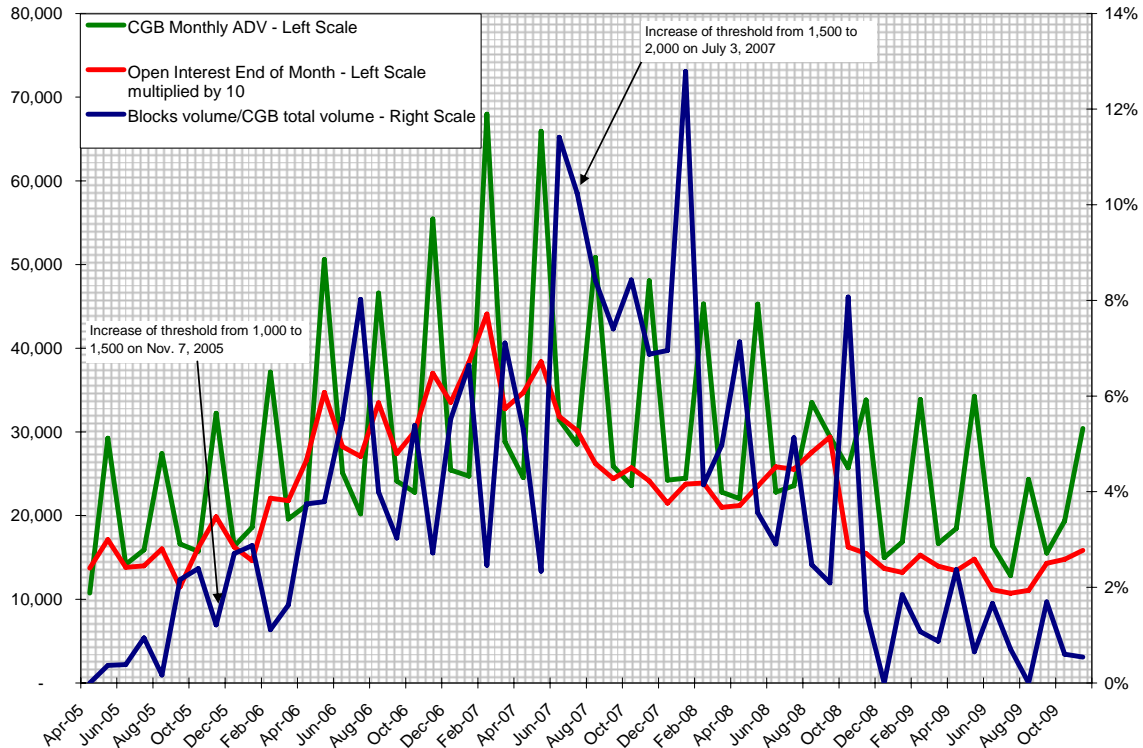
The proposed amendments are submitted to the Rules and Policies Committee of the Bourse for approval. Once the approval has been obtained, they will then be transmitted to the Autorité des marchés financiers (AMF) in accordance with the self-certification process and to the Ontario Securities Commission (OSC) for information. The proposed amendments will also be published for a 30-day comment period.

## **VII. ATTACHED DOCUMENTS**

Procedures applicable to the execution of block trades.

## VIII. APPENDIX

### MONTHLY AVERAGE DAILY VOLUME OF THE CGB FUTURES CONTRACT (LEFT SCALE) AND THE PROPORTION REPRESENTED BY BLOCK TRADES (RIGHT SCALE) FOR THE PERIOD OF APRIL 2005 TO NOVEMBER 2009



The following methodology demonstrates how we quantitatively determined the new threshold level.

#### METHODOLOGY

- We studied the CGB's monthly activity from Jan-Oct. 2009 from the Times & Sales data files.
- Transactions including block trades are ranked by decreasing order of size.
- From the largest to the lowest transaction size (the lowest corresponding to the level at which the transaction size does not impact significantly the market), we compute:
  - From the tick data file: Bid Price at transaction time, Ask Price at transaction time, Minimum Bid Price +/- 5 minutes off the transaction time, Maximum Ask Price +/- 5 minutes off the transaction time,
  - From the Times & Sales file: Average Transaction Size 15 minutes before, Average Transaction Size 15 minutes after and finally the Monthly Average Transaction Size.
- We verify if the transaction price is inside the Bid-Ask spread.
- We verify if the transaction price is inside the Minimum Bid-Maximum Ask spread in a period of +/- 5 minutes off the transaction time. The Minimum Bid-Maximum Ask

spread in a period of +/- 5 minutes off the transaction time will also tell us whether there is a price move within the period of +/- 5 minutes off the transaction time, e.g.: if the transaction can move market prices.

- If the Average Transaction Size 15 minutes before, or 15 minutes after the transaction is/are significantly higher than the Monthly Average Transaction Size, we can conclude that the transaction significantly impacts the market in terms of volume.
- For a given month, the upper limit is the lowest value of the transaction size for which the price will be outside of the Bid-Ask spread. The lower limit is the lowest value of the transaction size for which the price will be inside the Bid-Ask spread (Rules of rejection: 1. any transaction for which the size is higher than a block trade in a given month; 2. any block trade for which the price is inside the Bid-Ask spread).
- We compute the average of the monthly upper and lower limits. The upper limit corresponds to the optimal threshold for block trades.
- In order to evaluate the impact of block trades on volume, we apply the AMF method (decision No : 2004-SMV-0191): we compare Average cumulated volume before block (15 min.), Average cumulated volume before disclosure (15 min.), Average cumulated volume after divulgation (15 min.) and Average cumulated volume by 15 min. period (excluding blocks). See the results in table 2 below. For the 2008-2009 period, we chose a sample, the month of April 2009, where we recorded 4 block trades.

## RESULTS

- Based on table 1 below, we obtain an upper limit of 1,513 contracts and a lower limit of 1,129 contracts.
- Based on a market survey, the majority of market participants have suggested that the optimal threshold level for block trades should be established at 1,500 contracts.
- To conclude, the qualitative approach suggests a threshold of 1,500 and the quantitative approach confirms 1,500 contracts. We suggest a threshold in line with the quantitative approach. Remember that the preceding threshold increase has been made in two steps, from 1,000 to 1,500 and from 1,500 to 2,000. The decrease should be made by steps of 500 contracts, i.e. from 2,000 to 1,500 contracts.
- The analysis of the impact of block trades on volume illustrated in table 2 below shows that there is a significant activity before execution (1,015 cumulated volume on average for April 2009), before (788) and after (765) disclosure of block trades compare to Average cumulated volume by 15 min. period excluding blocks (438). It illustrates the recrudescence of hedging activity around the block trade. This is a good argument for blocks trades. Brokers involved in block trades need to hedge their position on the market place. Therefore, block trades indirectly bring liquidity to the market.

**TABLE 1: LARGE-SIZED CGB TRANSACTIONS RANKED IN DECREASING ORDER SIZE FOR THE PERIOD OF JAN-OCT 2009 AND THEIR CORRESPONDING RESULTS. NUMBERS HIGHLIGHTED IN YELLOW SIGNIFY THE MARKET HAS BEEN DISRUPTED.**

Date	Time	Trade Volume	External Symbol	Transaction Price	Bid Price at transaction time	Ask Price at transaction time	Min Bid Price +/- 5 minutes	Max Ask Price +/- 5 minutes	Average Transaction Size 15 minutes before	Average Transaction Size 15 minutes after	Monthly Average Transaction Size
20091023	140015	8848	CGBZ09	119.82	119.83	119.85	119.82	119.85	14.61	1.87	3.35
20091005	160252	5000	CGBZ09	121.95	121.92	122.1	120.7	122.75	1	N/A	3.35
20091007	152312	5000	CGBZ09	121.87	121.85	121.89	120.7	122.75	8.26	14	3.35
20091030	161228	4424	CGBZ09	120.55	120.45	120.5	120.45	120.5	4	N/A	3.35
20091021	91247	2442	CGBZ09	120.11	120.12	120.13	120.08	120.15	2.56	2.26	3.35
20091007	163144	1270	CGBZ09	121.8	121.78	121.82	121.78	121.82	1	N/A	3.35
20090917	121928	3539	CGBZ09	120.37	120.40	120.41	120.38	120.46	5.95	6.81	3.45
20090903	120446	2000	CGBZ09	120.71	120.69	120.70	120.67	120.72	2.28	2.75	3.45
20090918	85027	761	CGBZ09	120.54	120.54	120.58	120.48	120.61	1.89	2.54	3.45
20090820	151046	1764	CGBU09	121.35	121.50	121.53	121.44	121.55	2.93	24.80	3.27
20090824	122752	1764	CGBU09	120.75	121.04	121.05	121.00	121.07	4.44	25.70	3.27
20090824	122909	1764	CGBU09	120.75	121.02	121.04	121.00	121.07	15.06	12.73	3.27
20090818	115156	1144	CGBU09	121.29	121.22	121.24	121.21	121.28	1.86	2.37	3.27
20090806	134510	882	CGBU09	119.54	119.73	119.75	119.71	119.78	2.46	8.28	3.27
20090807	120231	882	CGBU09	119.30	119.11	119.12	119.07	119.16	6.48	19.93	3.27
20090807	120319	882	CGBU09	119.30	119.11	119.12	119.08	119.16	15.06	5.40	3.27
20090814	123723	882	CGBU09	120.81	120.72	120.78	120.63	120.85	7.46	1.34	3.27
20090825	112325	784	CGBU09	121.40	121.42	121.43	121.41	121.44	14.18	12.13	3.27
20090826	123604	662	CGBU09	121.62	121.31	121.32	121.29	121.45	4.37	4.15	3.27
20090824	122959	662	CGBU09	120.85	121.03	121.04	121.00	121.07	22.59	13.00	3.27
20090821	120602	655	CGBU09	121.10	120.97	121.00	120.93	121.05	2.60	1.79	3.27
20090812	162159	543	CGBU09	120.10	120.10	120.16	120.10	120.16	132.00	N/A	3.27
20090708	105731	2000	CGBU09	121.60	121.55	121.56	121.51	121.70	3.44	2.50	3.14
20090728	124406	1014	CGBU09	119.70	119.76	119.77	119.74	119.85	34.00	4.27	3.14
20090723	153607	906	CGBU09	119.49	119.52	119.58	119.51	119.59	47.50	14.33	3.14
20090717	131419	883	CGBU09	120.03	120.15	120.19	120.01	120.28	8.01	8.02	3.14
20090724	105404	882	CGBU09	119.57	119.55	119.59	119.52	119.61	5.30	8.39	3.14
20090616	95556	2000	CGBU09	119.88	119.89	119.90	119.78	120.02	2.63	1.64	3.01
20090616	122335	2000	CGBU09	120.22	120.29	120.30	120.20	120.33	1.56	1.83	3.01
20090623	92719	2000	CGBU09	120.35	120.44	120.45	120.37	120.46	1.91	1.89	3.01
20090609	134656	1764	CGBU09	119.40	119.31	119.33	119.29	119.39	1.50	2.43	3.01
20090616	161347	1764	CGBU09	119.80	120.35	120.50	120.05	120.50	29.66	N/A	3.01
20090622	111626	1374	CGBU09	120.00	119.97	120.00	119.95	120.02	2.81	2.63	3.01
20090506	85533	2300	CGBM09	124.10	124.11	124.13	124.06	124.19	3.43	3.55	5.37
20090514	85900	2168	CGBM09	124.08	124.06	124.08	124.03	124.17	2.13	2.43	5.37
20090508	104020	1312	CGBM09	122.55	122.92	122.93	122.85	123.05	3.16	5.13	5.37
20090506	141522	1003	CGBM09	124.20	124.00	124.03	124.00	124.20	2.55	1.90	5.37
20090526	115117	968	CGBU09	121.22	121.22	121.28	121.22	121.34	2.83	2.98	5.37
20090403	91617	2582	CGBM09	125.72	125.84	125.85	125.79	125.89	3.88	3.47	3.84
20090420	131840	2501	CGBM09	125.92	125.83	125.85	125.69	125.90	5.53	5.75	3.84
20090416	151537	2405	CGBM09	125.25	125.11	125.20	125.10	125.25	37.66	188.80	3.84
20090422	124838	2186	CGBM09	125.30	125.77	125.80	125.73	125.85	3.57	3.29	3.84
20090422	160925	2186	CGBM09	125.25	125.40	125.47	125.40	125.47	7.63	3.31	3.84
20090421	111442	2095	CGBM09	126.10	126.13	126.17	126.10	126.21	3.04	5.20	3.84
20090428	104704	2000	CGBM09	124.48	124.53	124.54	124.51	124.60	4.12	4.38	3.84
20090429	104925	1714	CGBM09	124.17	124.23	124.26	124.22	124.32	6.37	3.16	3.84
20090420	154959	1312	CGBM09	126.00	125.97	126.01	125.82	126.03	5.93	33.52	3.84
20090306	95123	3205	CGBM09	125.82	125.83	125.89	125.71	125.95	5.64	2.74	3.84
20090331	141306	2879	CGBM09	126.48	126.66	126.70	126.62	126.71	2.95	10.29	3.84
20090313	140540	1836	CGBM09	125.70	126.31	126.36	126.21	126.37	34.38	3.03	3.84
20090327	120200	1748	CGBM09	125.55	125.52	125.55	125.48	125.58	8.35	4.57	3.84
20090209	91129	2478	CGBH09	124.00	123.92	123.95	123.92	124.01	3.95	3.03	3.15
20090220	85217	2390	CGBH09	126.38	126.31	126.33	126.25	126.41	6.17	5.76	3.15
20090220	104852	2056	CGBH09	126.16	126.16	126.17	126.01	126.21	3.16	7.50	3.15
20090225	130816	1307	CGBH09	125.94	125.31	125.36	125.18	125.47	5.62	7.16	3.15
20090205	124758	1307	CGBH09	124.07	123.96	123.98	123.92	124.14	2.80	2.00	3.15
20090206	133123	1122	CGBH09	124.31	124.31	124.41	124.08	124.48	1.96	2.48	3.15
20090106	124644	2250	CGBH09	124.90	124.88	124.92	124.77	124.93	6.12	5.31	3.99
20090114	85631	2236	CGBH09	127.05	127.27	127.30	127.15	127.34	4.15	3.33	3.99
20090113	100836	2041	CGBH09	126.30	126.21	126.23	126.19	126.34	3.81	5.07	3.99
20090123	124903	1835	CGBH09	126.38	125.59	125.61	125.50	125.69	3.97	37.76	3.99
20090123	125131	1742	CGBH09	125.70	125.55	125.59	125.48	125.66	29.08	6.90	3.99
20090130	120628	1525	CGBH09	124.43	124.27	124.30	124.16	124.31	11.17	2.00	3.99
20090130	153006	1307	CGBH09	124.11	124.01	124.16	123.86	124.20	89.28	13.40	3.99

Upper limit: 1513  
Lower limit: 1129

Legend:  = Impact on Price or Volume



**TABLE 2: IMPACT ON VOLUME**

CGB	Block trades average volume	Average cumulated volume before block (15 min.)	Average cumulated volume before divulgation (15 min.)	Average cumulated volume after divulgation (15 min.)	Average cumulated volume by 15 min. period (excluding blocks)
April 2009 Average	2,295	1,015	788	765	438
2007-2008 Average	3,065	1,546	1,941	1,497	827
2006-2007 Average	2,466	1,076	1,339	1,333	895
2005-2006 Average	1,312	766	691	823	692
	2007-2008	2006-2007	Apr-09		
Blocks total volume	548,620	384,704	9,178		
Total volume of trading days including blocks	6,827,838	3,056,595	19,847		
Total volume	8,013,942	9,176,722	387,586		
% blocks volume / Total volume of trading days including blocks	8%	13%	46%		
% blocks volume / Total volume	7%	4%	2%		

## PROCEDURES FOR THE EXECUTION OF BLOCK TRADES

- a) Once a block trade has been arranged, in accordance with the predetermined minimum quantity threshold level as determined and published by the Bourse, details of the block trade must be reported to the Bourse by contacting a market official of the Bourse's Market Monitoring Department at 1-888-693-6366 or at (514) 871-7871 within the period of time prescribed by the Bourse.
- b) Approved participants for both the seller and buyer must complete and submit the Block Trade Reporting Form (Attachment I) or such other notification as prescribed by the Bourse to a market official of the Bourse's Market Monitoring Department for validation.
- c) A market official will check the validity of the block trade details submitted by the approved participant(s).
- d) Confirmation by a market official of a block trade transaction will not preclude the Bourse from initiating disciplinary procedures in the event that the transaction is subsequently found to have been made other than in compliance with the rules.
- e) Once the block trade has been validated, the following information with respect to the block trade will be disseminated by the Bourse:
  - i) date and time of transaction;
  - ii) security(ies) or derivative instrument(s) and contract month(s);
  - iii) price of each contract month(s) and strike price(s) (as applicable); and
  - iv) volume of each contract month.
- f) Upon request by the Bourse the approved participant who arranges a block trade must provide satisfactory evidence that the block trade has been arranged in accordance with the Rules of the Bourse. Failure to provide satisfactory evidence of compliance with these Rules may result in the initiation of disciplinary action.

In accordance with article 6380 of the Rules of Bourse de Montréal Inc. (the “Bourse”), the following are the eligible securities and derivative instruments, the relevant prescribed time delays and the minimum quantity thresholds for the execution of block trades.

ELIGIBLE SECURITIES AND DERIVATIVE INSTRUMENTS	PRESCRIBED TIME DELAY	MINIMUM QUANTITY THRESHOLD
	(As soon as practicable and in any event within the following time delay)	
<b>Thirty-day Overnight “Repo” Rate Futures Contracts (ONX):</b>	15 minutes	1,000 contracts
<b>Ten-year Government of Canada Bond Futures Contracts (CGB):</b>	15 minutes	2,01,500 contracts
<b>Two-year Government of Canada Bond Futures Contracts (CGZ):</b>	15 minutes	500 contracts
<b>Thirty-year Government of Canada Bond Futures Contracts (LGB)</b>	15 minutes	500 contracts
<b>Five-year Government of Canada Bond Futures Contracts (CGF)</b>	15 minutes	500 contracts
<b>Options on Three – month Canadian Bankers Acceptance Futures Contracts (OBX)</b>	15 minutes	2,000 contracts

**Block Trade Reporting Form**

Approved participants must complete all sections of this form legibly and accurately.

This form is to be completed and faxed to Market Monitoring at (514) 871-3592.

A market official can be reached at 1-888-693-6366 or at (514) 871-7871.

<b>TIME AND DATE OF TRADE:</b>	
<b>EXECUTING PARTICIPANT NAME AND TRADING ID (BUY):</b>	
<b>CLEARING FIRM NAME AND ID (BUY):</b>	
<b>EXECUTING PARTICIPANT NAME AND TRADING ID (SELL):</b>	
<b>CLEARING FIRM NAME AND ID (SELL):</b>	
<b>CONTACT PHONE NUMBER:</b>	
<b>CONTACT FAX NUMBER OR E-MAIL ADDRESS:</b>	

Derivative Instruments	Future Contract/ Call / Put	Contract Month	Option Strike Price (if applicable)	Number of Contracts	Price	Strategy Type* (if applicable)

For Montréal Exchange Staff Only:

**Time and Date of receipt:**  
\_\_\_\_\_

**Montréal Exchange authorized signature:**  
\_\_\_\_\_

The details on this form are accepted by the Montréal Exchange strictly on the understanding that the Montréal Exchange accepts no responsibility nor liability for the accuracy or completeness of the details as provided by the approved participant.

\* Each leg of a strategy trade should be listed separately.