

NOTICE TO MEMBERS

N° 076-24

June 5, 2024

REQUEST FOR COMMENTS

AMENDMENTS TO THE RULES OF THE CANADIAN DERIVATIVES CLEARING CORPORATION REGARDING VOLUNTARY WITHDRAWAL AND THE LIMITED LIABILITY OF CLEARING MEMBERS

On **April 30, 2024**, the Board of Directors of Canadian Derivatives Clearing Corporation (“**CDCC**”) approved certain amendments to the rules of CDCC (the “**Rules**”) to limit withdrawing Clearing Members’ exposure to one Default Management Period (“**DMP**”) following the closing of their outstanding positions and to consolidate in the Rules all aspects of the definition of the DMP.

Please find enclosed an analysis document as well as the proposed amendments.

Process for Changes to the Rules

CDCC is recognized as a clearing house under section 12 of the *Derivatives Act* (Québec) by the Autorité des marchés financiers (“**AMF**”) and as a recognized clearing agency under section 21.2 of the *Securities Act* (Ontario) by the Ontario Securities Commission (“**OSC**”).

The Board of Directors of CDCC has the power to approve the adoption or amendment of the Rules of CDCC. Amendments are submitted to the AMF in accordance with the self-certification process and to the OSC in accordance with the process provided in the Recognition Order.

Comments on the proposed amendments must be submitted before **July 5, 2024**. Please submit your comments to:

Maxime Rousseau-Turenne
Legal Counsel
Canadian Derivatives Clearing Corporation
1800-1190 av. des Canadiens-de-Montréal, P.O. Box 37
Montreal, Quebec H3B 0G7
Email: legal@tmx.com

A copy of these comments shall also be forwarded to the AMF and to the OSC to:

M ^e 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 Fax : (514) 864-8381 E-mail: consultation-en-cours@lautorite.qc.ca	Manager, Market Regulation Market Regulation Branch <i>Ontario Securities Commission</i> Suite 2200, 20 Queen Street West Toronto, Ontario, M5H 3S8 Fax: 416-595-8940 Email: marketregulation@osc.gov.on.ca
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For any question or clarification, Clearing Members may contact Maxime Rousseau-Turenne, Legal Counsel, at maxime.rousseauturenne@tmx.com

George Kormas
President

Canadian Derivatives Clearing Corporation

100 Adelaide Street W 1800-1190 av des Canadiens-de-Montréal
3rd Floor P.O. Box 37
Toronto ON M5H 1S3 Montreal, Quebec H3B 0G7
416.367.2470 514.871.3545
www.cdcc.ca



AMENDMENTS TO THE RULES OF THE CANADIAN DERIVATIVES CLEARING CORPORATION REGARDING VOLUNTARY WITHDRAWAL AND THE LIMITED LIABILITY OF CLEARING MEMBERS

I. DESCRIPTION

Further to various discussions held by the Canadian Derivatives Clearing Corporation (“CDCC”) with Clearing Members (“CMs”) in late 2022 pertaining to the potential uncapped liability of CMs towards CDCC in the event of successive CM defaults, as well as to the length of the Default Management Period (“DMP”), CDCC hereby proposes to amend its rules (the “Rules”) to limit withdrawing CMs’ exposure to one Default Management Period following the closing of the CM’s outstanding positions and to consolidate in the Rules all aspects of the definition of the DMP (the “Proposed Change”).

The Proposed Change aligns with similar provisions in other jurisdictions and reflects in-depth discussions held between CDCC and its CMs. Through this process, CDCC considered insights from its stakeholders, while also considering the impact of the Proposed Change on its resiliency. The Proposed Change will remove current ambiguity in the Rules related to withdrawing CMs’ exposure to multiple DMPs and add further clarity and homogenization to the definition of said DMP.

Unless otherwise defined herein, any defined term used in this analysis will have the meaning described in the Rules.

II. PROPOSED AMENDMENTS

CDCC hereby proposes to amend Section A-1A09 in Rule A-1A of the Rules to clarify current CDCC provisions with regards to the voluntary withdrawal of CMs concurrently to a Default Management Period, and to their potential liability towards CDCC further to such withdrawal. More specifically, CDCC proposes to modify Paragraph A-1A09(2) to specify that, should the withdrawal of a CM become effective while a DMP is ongoing, such withdrawal will be postponed and become effective after the end of the DMP, on such date where the CM will have satisfied all its obligations towards CDCC (including the closing of all of the withdrawing CM’s outstanding positions at CDCC), or on the date agreed upon by CDCC. Secondly, CDCC proposes to introduce Paragraph A-1A09(3) to clarify that a withdrawing CM’s liability towards CDCC will be limited to the obligations arising from the DMPs ongoing while the CM still has outstanding positions at CDCC. Accordingly, once all of the withdrawing CM’s positions at CDCC have been closed, the CM shall be liable to CDCC for a maximum of one additional Default Management Period initiated after such close-out, if any.

Additionally, CDCC proposes some minor adjustments to Section A-411 of the Rules to consolidate in the Rules the definition of Default Management Period and align it with the DMP provisions of its Operations Manual.

The Proposed Change is provided herein in Appendix “A”.

III. ANALYSIS

a. Background

In the course of Q4-2022, CDCC received comments from Clearing Members pertaining to the potential uncapped liability of CMs towards CDCC in the event of defaults subsequent to the submission of a voluntary withdrawal notice to CDCC pursuant to Section A-1A09 of the Rules. Further to these comments, CDCC decided to assess the opportunity to review applicable provisions in its Rules by conducting benchmarking analyses against the provisions of other central counterparty clearing houses (“CCPs”) and organize further discussion sessions with its CMs.

The results of CDCC’s review were that ambiguity could be removed from its Rules, as the limit of the obligations of a CM towards CDCC resulting from DMP(s) subsequent to the submission by the CM to CDCC of a voluntary withdrawal notice is not currently defined. Further ambiguity was found in that the Rules meanwhile provide that CMs need to wait for the prescribed 30-day withdrawal period, even if their withdrawal notice were submitted in the course of an ongoing DMP. In light of the situation, some CMs proposed that CDCC introduce a cooling-off period following a DMP in the same way some CCPs - including those of the CME Group and LCH Group - are implementing. However, since introducing such a cooling-off period may reduce the financial resources available to a CCP to manage additional defaults, both CDCC and its CMs considered it may have a negative impact on CDCC’s sustainability and market resilience (see *section III c) below*). As a solution to maintain CDCC’s resiliency, but to still allow CMs to better quantify their maximum exposure when withdrawing, CDCC decided to clarify the language in the Rules to limit exposure without the need for a cooling-off period.

b. Objectives

The objective of the Proposed Change is to address and correct CMs’ potential uncapped liability in the event of DMP(s). CDCC will enhance the language in the Rules defining the DMP and clarify the language used in Rule A-1A09 - *Voluntary Withdrawal* to allow CMs to better quantify their maximum exposure to CDCC, while maintaining CDCC’s sustainability and market resilience.

c. Comparative Analysis

CDCC conducted a thorough comparative analysis against other global CCPs. Most of the CCPs have introduced in their rules a cooling-off period, which consists of a period where a CCP cannot call for cash assessments from CMs over the cap, regardless of whether additional CMs default. Currently, the CMs’ liability in CDCC is capped at 200% per DMP, but CDCC has not introduced a formal cooling-off period, exposing CMs to liability in the event of additional

defaults. As CDCC only maintains cover 1 status,¹ while most of the CCPs in the analysis maintain cover 2 status², the Default Waterfall Resources (the “DWR”) calibration by CDCC is based on the assumption of covering the default of one Clearing Member. In the case of multiple defaults, CMs need to replenish the DWR after the DMPs. Therefore, since CDCC has a more concentrated membership, it has a higher exposure risk compared to other CCPs in the case of multiple CM defaults. Based on the rationale above, CDCC decided not to implement a cooling-off period.

From the perspective of voluntary withdrawal, most CCPs, including CDCC, require members to be responsible for their clearing obligations until the resignation process is fully completed. The resignation process is only accepted if all clearing positions have been extinguished. Moreover, it is common practice for most CCPs that members also continue to be responsible for any further contributions to their default fund if a default is declared following the resignation of a clearing member. The Proposed Change to further clarify the language used in CDCC Rules regarding the Default Management Period and limited liability of withdrawing CMs aligns with these practices.

¹ Cover 1 status refers to a default fund size that covers the default of the largest clearing member in extreme but plausible situations.

² Cover 2 status refers to a default fund size that covers the default of the two largest clearing members in extreme but plausible situations.

The following table shows the benchmarking analysis held against other global CCPs.

	CME (Cover 2)	LCH (Cover 2)	SGX (1 largest & 2 smallest)	ASX (Cover 2)	CC&G (Italy) (Cover 2)	B3 (Brazil) (Cover 2)
Default / Cool-off period	5 business days after the default of a clearing member	30 calendar days from default management completion notice	90 calendar days after the default of a clearing member	Default management completion period + 22 calendar days cooling-off period	Default management completion period (No cool-off period)	Default management completion period + 20 business days cooling-off period
Cap on replenishment for single and multiple independent DMP	- 2.75 x Base guaranty fund - 5.5 x Base guaranty fund in case of multiple defaults	- 1x contribution - Up to 3 defaults in any 6 months	- 1x contribution - 1x contribution per default for multiple defaults	- 2x contribution	- Replenishment to minimum default fund, new default fund calculated 30 days after default.	- 3x contribution
Resignation during the DMP	If the withdrawing conditions are satisfied, the clearing member is not subject to any residual assessment to cover losses for defaults occurring after the related base cooling-off period	Required to maintain some or all of its contribution until after the completion of the default management process (even if the resignation effective date might occur prior to the end of process)	30 days' notice, no information regarding the default found	Participant to send notice to ASX. Resignation becomes effective on the last day of the default period.	The intention of resignation during a 2-day period. Effective 20 days after if positions are closed.	Participant to send notice to B3. Resignation becomes effective on the last day of the default period if conditions are met.
Impact of resignation on replenishment	Liable for assessments and replenishment till resignation effective	Not liable for replenishment if resign and close out whilst replenishment obligation suspended.	Liable for defaults declared before resignation effective. Capped at 2x clearing participants' contribution and further assessment of time of resignation	No replenishment once CCP accepts resignation (even if not effective yet).	Required to maintain Cover 2 level of funds. Not liable to replenish new default fund	If resignation conditions are met, participant is not subjected to replenishment at the end of the cooling-off period.

d. Analysis of Impacts

i. Impacts on Market

The Proposed Change aims to provide further clarification to the current CDCC withdrawal process and Default Management Period. The Proposed Change will remove ambiguity identified by CMs and allow them to better quantify their maximum exposure to CDCC, as well as incentivize them to proactively manage their positions after submitting a voluntary withdrawal request to CDCC pursuant to Section A-1A09. The Proposed Change will have no further impacts on the market and its participants.

ii. Impacts on Technology

The Proposed Change does not impact CDCC's clearing system (SOLA). Existing features will be used to manually resize Clearing Fund ("CF") requirements, including, when applicable, the exclusion of a Clearing Member from the CF sizing when selecting the historical worst stressed member and affiliate level shortfall within the CF lookback period and/or the exclusion of a Clearing Member from the distribution of the calculated global CF.

iii. Impacts on Trading Functions

The Proposed Change will have no impact on Bourse de Montréal Inc.'s trading systems or rules.

iv. Public Interest

CDCC considers the Proposed Change to be in the interest of the public as it will remove ambiguity from its Rules and align them with the best practices of other clearing houses, while remaining compliant with PFMI requirements, the whole at the request of its own Clearing Members. The Proposed Change will allow CMs to better quantify their maximum exposure, while continue to maintain CDCC's sustainability and market resilience.

IV. PROCESS

The Proposed Change, including this analysis, must be approved by CDCC's board of directors and submitted to the Autorité des marchés financiers, in accordance with the regulatory self-certification process, and to the Ontario Securities Commission in accordance with the rules stated in Appendix "A" of Schedule "A" CDCC Recognition Order dated June 15, 2023. The Proposed Change and analysis will also be submitted to the Bank of Canada in accordance with the Oversight Agreement. Subject to public comments and following regulatory approval, the Proposed Change is expected to take effect during Q3-2024.

APPENDIX A: AMENDMENTS TO THE CDCC RULES

BLACKLINE VERSION

[...]

Section A-1A09 - Voluntary Withdrawal

(1) A Clearing Member may, at any time, notify the Corporation that it wishes to withdraw as a Clearing Member of the Corporation, by giving a minimum of 30 ~~days~~^{days} prior written notice. The Clearing Member shall cease to be a Clearing Member on the later of (a) the date of expiry of the notice period ~~or~~, (b) the date, as determined by the Corporation, on which the Clearing Member has satisfied all of its obligations toward the Corporation and any applicable requirements for withdrawal, including the closing of all the Clearing Member's Open Positions and the performance of any obligation arising in connection with the closing of such Open Positions; or (c) the date on which the Corporation agrees to the withdrawal.

(2) If the withdrawal ~~Withdrawal~~ of a Clearing Member ~~which has provided a prior notice of withdrawal to the Corporation, in the event that becomes effective while~~ a Default Management Period is ~~initiated before the effective date of ongoing, such~~ withdrawal, shall not occur and shall be postponed until the end of the Default Management Period, and ~~such the~~ Clearing Member shall cease to be a Clearing Member ~~at on~~ the date, as determined by the Corporation, on which the Clearing Member has satisfied all of its obligations toward the Corporation, or the date on which the Corporation agrees to the withdrawal.

(3) Notwithstanding the provisions of Section A-1A09(2), during the prior notice period referred to under Section A-1A09(1), the Clearing Member shall be liable to the Corporation for:

(a) while the Clearing Member has outstanding positions, the obligations resulting from all Default Management Periods initiated during such prior notice period referred to under Section A-1A09(1);

(b) once all of the Clearing Member's positions have been closed, the obligations resulting from one (1) Default Management Period initiated after such close-out during the prior notice period referred to under Section A-1A09(1).

(4) The Corporation shall notify all Clearing Members upon receipt of a notice of withdrawal pursuant to Section A-1A09(1).

(5) Upon receipt of a notice of withdrawal pursuant to Section A-1A09(1) from a Non-Conforming Member, the Corporation shall promptly notify the Board, all Clearing Members, the Exchanges, the self-regulatory organization or agency having jurisdiction over the activities of such Non-Conforming Member and any regulatory agency having jurisdiction over the activities of the Corporation and any other entity or organization that the Corporation may consider appropriate, that it has received a notice of withdrawal from such Non-Conforming Member.

[...]

Section A-411 - Default Management Period

(1) A Default Management Period means the period:

(a) commencing on the day that the Corporation declares the suspension of a Clearing Member, and

(b) concluding on the Default Management Period End Date;

provided, however, that if the Corporation declares the suspension of a Clearing Member when a Default Management Period is ongoing due to the prior suspension of another Clearing Member, multiple Clearing Members' suspensions will be processed in a single Default Management Period.

(2) The Default Management Period End Date shall occur on the Business Day following the declaration by the Corporation that [the Default Management Process is completed and:](#)

(a) the obligations, losses or expenses incurred or sustained by the Corporation in connection with the suspension(s) of Non-Conforming Member(s) are known, or can reasonably be determined, and have been satisfied or otherwise settled; or

(b) any of the actions, rights or remedies available to the Corporation with respect to the suspension of any Clearing Member that were deemed necessary by the Corporation have been taken; and

(c) ~~the Default Management Period with respect to the suspended Clearing Member(s) has been completed.~~ [the Corporation has successfully reestablished a matched book.](#)

[...]

AMENDMENTS TO THE CDCC RULES

CLEAN VERSION

[...]

Section A-1A09 - Voluntary Withdrawal

(1) A Clearing Member may, at any time, notify the Corporation that it wishes to withdraw as a Clearing Member of the Corporation, by giving a minimum of 30 days prior written notice. The Clearing Member shall cease to be a Clearing Member on the later of (a) the date of expiry of the notice period; (b) the date, as determined by the Corporation, on which the Clearing Member has satisfied all of its obligations toward the Corporation and any applicable requirements for withdrawal, including the closing of all the Clearing Member's Open Positions and the performance of any obligation arising in connection with the closing of such Open Positions; or (c) the date on which the Corporation agrees to the withdrawal.

(2) If the withdrawal of a Clearing Member becomes effective while a Default Management Period is ongoing, such withdrawal shall not occur and shall be postponed until the end of the Default Management Period, and the Clearing Member shall cease to be a Clearing Member on the date, as determined by the Corporation, on which the Clearing Member has satisfied all of its obligations toward the Corporation, or the date on which the Corporation agrees to the withdrawal.

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(a) commencing on the day that the Corporation declares the suspension of a Clearing Member, and

(b) concluding on the Default Management Period End Date;

provided, however, that if the Corporation declares the suspension of a Clearing Member when a Default Management Period is ongoing due to the prior suspension of another Clearing Member, multiple Clearing Members' suspensions will be processed in a single Default Management Period.

(2) The Default Management Period End Date shall occur on the Business Day following the declaration by the Corporation that the Default Management Process is completed and:

(a) the obligations, losses or expenses incurred or sustained by the Corporation in connection with the suspension(s) of Non-Conforming Member(s) are known, or can reasonably be determined, and have been satisfied or otherwise settled; or

(b) any of the actions, rights or remedies available to the Corporation with respect to the suspension of any Clearing Member that were deemed necessary by the Corporation have been taken; and

(c) the Corporation has successfully reestablished a matched book.

[...]