

CMRA Regulation 91-501
Derivatives and Strip Bonds

PART 1 DEFINITIONS AND INTERPRETATION

1. Definitions
2. Interpretation

PART 2 EXEMPT DERIVATIVES

3. Registration and prospectus exemptions for certain derivatives

PART 3 EXCHANGE CONTRACTS

4. Proficiency
5. Risk disclosure statement
6. Registration exemption – International dealer
- 7 General condition to international dealer registration requirement exemption
8. Registration exemption – International adviser
9. General condition to international adviser registration requirement exemption

PART 4 OVER-THE-COUNTER DERIVATIVES

10. Registration and prospectus exemptions

PART 5 STRIP BONDS

11. Removal of registration and prospectus exemptions
12. Registration and prospectus exemptions

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PART 1 DEFINITIONS AND INTERPRETATION

1. Definitions

In this Regulation,

“Accord” means the International Convergence of Capital Measurement and Capital Standards issued by the Committee on Banking Regulations and Supervisory Practices (Basle, Switzerland: July 1988) (Committee on Banking Supervision) or any successor standards;

“aggregate consolidated gross revenue” does not include the gross revenue of an affiliate of the adviser if the affiliate is registered in a jurisdiction of Canada;

“CFA Charter” has the same meaning as in National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*;

“designated foreign jurisdiction” means the United Kingdom of Great Britain and Northern Ireland or the United States of America;

“designated rating” has the same meaning as in National Instrument 81-102 *Investment Funds*;

“designated rating organization” has the same meaning as in National Instrument 81-102 *Investment Funds*;

“DRO affiliate” has the same meaning as in National Instrument 25-101 *Designated Rating Organizations*;

“first-time purchaser” means, at any specific time, a purchaser of a strip bond to whom a copy of a then-current information statement has not been delivered;

“information statement” means an information statement in the form of Form 91-501F3 *Strip Bonds and Strip Bond Packages Information Statement* describing the investment attributes of strip bonds;

“non-Canadian exchange contract” means an exchange contract traded on an exchange that is located outside of Canada and cleared through one or more clearing agencies located outside of Canada;

“permitted client” has the same meaning as in National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*;

“qualified party” means any of the following

- (a) a bank to which the *Bank Act* (Canada) applies;
- (b) the Business Development Bank of Canada continued under the *Business Development Bank of Canada Act* (Canada);

- (c) a bank subject to the regulatory regime of a country that is a member of the Accord or a country that is not an initial signatory to the Accord but has adopted the regulatory and supervisory rules set out in the Accord;
- (d) a credit union central or a federation of caisses populaires or any credit union or regional caisse populaire located, in each case, in Canada;
- (e) a loan or trust corporation registered under the loan and trust corporations legislation of a province or territory of Canada or under the *Trust and Loan Companies Act* (Canada);
- (f) a loan or trust company subject to the regulatory regime of a country that is a member of the Accord or a country that is not an initial signatory to the Accord but has adopted the regulatory and supervisory rules set out in the Accord for banks that are subject to the country's banking regulation and supervision;
- (g) an insurance company licensed to do business in Canada or a province or territory of Canada;
- (h) an insurance company subject to the regulatory regime of a country that is a member of the Accord or a country that is not an initial signatory to the Accord but has adopted the regulatory and supervisory rules set out in the Accord for banks that are subject to the country's banking regulation and supervision;
- (i) a pension fund that is regulated by the Office of the Superintendent of Financial Institutions (Canada) or a provincial or territorial pension supervisory authority;
- (j) a mutual fund or non-redeemable investment fund if each investor in the fund is a qualified party;
- (k) a mutual fund, if the investment portfolio of the fund is managed by a person that is registered under the Act or the securities legislation of another province or territory of Canada as a portfolio manager;
- (l) a non-redeemable investment fund, if the investment portfolio of the fund is managed by a person that is registered under the Act or the securities legislation of another province or territory of Canada as a portfolio manager;
- (m) a person registered under the Act or the securities legislation of another province or territory of Canada as an investment dealer or restricted dealer that is permitted to trade in derivatives;
- (n) a person registered under the Act or the securities legislation of another province or territory of Canada as a portfolio manager or a restricted portfolio manager that is permitted to advise on derivatives;
- (o) a person that buys, sells, trades, produces, markets, brokers or otherwise uses a commodity in its business and that enters into an OTC derivative, provided that a material component of the underlying interest of the OTC derivative is

- (i) a commodity that the person buys, sells, trades, produces, markets, brokers, or otherwise uses in its business,
 - (ii) a related commodity, security or variable,
 - (iii) a commodity, security or variable that directly or indirectly affects the commodity that the person buys, sells, trades, produces, markets, brokers or otherwise uses in its business,
 - (iv) a commodity, security or variable for which there is a high degree of correlation between the movement in its value and the movement in the value of the commodity that the person buys, sells, trades, produces, markets, brokers, or otherwise uses in its business, or
 - (v) another OTC derivative, where a material component of the underlying interest of that OTC derivative is a commodity, security or variable referred to in sub-paragraphs (i) to (iv) above;
- (p) a person that
- (i) together with its affiliates has entered into one or more OTC derivatives with counterparties that are not its affiliates, if
 - (A) the aggregate value of the notional principal amounts of the OTC derivatives is at least \$1 billion (or its equivalent), and
 - (B) any of the OTC derivatives was outstanding on any day during the previous 15 month period, or
 - (ii) together with its affiliates had total gross marked-to-market positions of or equivalent to at least \$100 million aggregated across counterparties, in one or more OTC derivatives on any day during the previous 15 month period;
- (q) an individual who, either alone or jointly with the individual's spouse, has a net worth, as shown in the individual's most recent statement of assets and liabilities, of at least \$5 million (or its equivalent in another currency), excluding the value of any principal residence;
- (r) a company, partnership, unincorporated association, organization or trust, with total assets, as shown in the balance sheet for its most recently completed financial year end (prepared in accordance with generally accepted accounting principles and audited, if the party has produced an audited balance sheet for that financial year end), in excess of \$25 million (or its equivalent in another currency);
- (s) a person that, directly or indirectly, is wholly-owned by any of the persons described in paragraphs (a), (b), (c), (d), (e), (f), (g), (h), (m), (n), (q) and (r);
- (t) a person that, directly or indirectly, wholly owns any of the persons described in paragraphs (a), (c), (d), (e), (f), (g), (h), (m), (n) and (r);

- (u) a direct or indirect wholly-owned subsidiary of a person described in paragraph (t);
- (v) Her Majesty in right of Canada or any province or territory of Canada and any crown corporation, instrumentality or agency of Canada or a province or territory;
- (w) a national government of a country or any political division of a country and any instrumentality or agency of that government or political division;
- (x) a Canadian municipality with a population in excess of 50,000 and any Canadian provincial or territorial capital city;
- (y) a person whose obligations in respect of the OTC derivative are fully guaranteed by another qualified party; and
- (z) a person that is designated as a qualified party by the Authority;

“strip bond” means

- (a) an interest in an amount of principal or interest payable under an underlying bond, or in a pool of amounts of principal or interest payable under one or more underlying bonds, in either case in which the sole entitlement of the holder of the interest is to receive, at a specific future date, a sum certain in money that is fixed at the date of issue of the interest;
- (b) a security that solely consists of at least two of the interests referred to in paragraph (a) and that is not an underlying bond; or
- (c) a deposit receipt or other certificate representing an interest referred to in paragraph (a) or a security referred to in paragraph (b); and

“underlying bond” means

- (a) a bond, debenture or other evidence of indebtedness of or guaranteed by the Government of Canada or by a province or territory of Canada; or
- (b) a bond, debenture or other evidence of indebtedness of or guaranteed by the government of a foreign jurisdiction if the evidence of indebtedness has a designated rating from a designated rating organization or its DRO affiliate.

2. Interpretation

Exchange contracts prescribed not to be securities

- (1) For the purposes of the definition “security” in section 2 of the Act, exchange contracts are prescribed not to be securities.

OTC derivatives prescribed to be securities

- (2) OTC derivatives that are not otherwise securities are prescribed under section 41 of the Act to be securities for the purpose of Part 5 of the Act and related Regulations.

Interpretation of “qualified party” and “permitted client”

- (3) In this Regulation,
- (a) a party to an OTC derivative is a qualified party or a permitted client if that party is a qualified party or a permitted client at the time the party enters into the OTC derivative; and
 - (b) a party entering into an OTC derivative with a party who claims to be a qualified party or a permitted client is entitled to rely on a representation by that party that the party is a qualified party or a permitted client, unless the first party believes or has reasonable grounds to believe that the representation is false.

Interpretation of “acting as principal”

- (4) In this Regulation, a party referred to in paragraph (e), (f), (g), (h) or (n) of the definition of “qualified party” and paragraph (j) or (k) of the definition of “permitted client” is deemed to be acting as principal when it acts as an agent or trustee for accounts that are fully managed by it.

PART 2 EXEMPT DERIVATIVES

3. Registration and prospectus exemptions for certain derivatives

Provided that the contract or instrument is not also a security or an exchange contract, the registration requirement and the prospectus requirement do not apply in respect of a trade in a derivative that is

- (a) regulated by
 - (i) gaming control legislation of Canada or a jurisdiction of Canada, or
 - (ii) gaming control legislation of a foreign jurisdiction, if the contract or instrument
 - (A) is entered into outside of Canada,
 - (B) is not in violation of legislation of Canada or a CMR Jurisdiction, and
 - (C) would be regulated under gaming control legislation of Canada or a CMR Jurisdiction if it had been entered into in a CMR Jurisdiction;

- (b) an insurance or annuity contract entered into
 - (i) with an insurer holding a licence under insurance legislation of Canada or a jurisdiction of Canada and regulated as insurance under that legislation, or
 - (ii) outside of Canada with an insurer holding a licence under insurance legislation of a foreign jurisdiction, if it would be regulated as insurance under insurance legislation of Canada or a CMR Jurisdiction if it had been entered into in a CMR Jurisdiction;
- (c) a contract or instrument for the purchase and sale of currency that
 - (i) except where all or part of the delivery of the currency referenced in the contract or instrument is rendered impossible or commercially unreasonable by an intervening event or occurrence not reasonably within the control of the parties, their affiliates or their agents, requires settlement by the delivery of the currency referenced in the contract or instrument,
 - (A) within two business days, or
 - (B) after two business days provided that the contract or instrument was entered into contemporaneously with a related security trade and the contract or instrument requires settlement on or before the relevant security trade settlement deadline,
 - (ii) is intended by the counterparties, at the time of the execution of the transaction, to be settled by the delivery of the currency referenced in the contract within the time periods set out in subparagraph (i), and
 - (iii) does not allow for the contract or instrument to be rolled over;
- (d) a contract or instrument for delivery of a commodity other than cash or currency that
 - (i) is intended by the counterparties, at the time of execution of the transaction, to be settled by delivery of the commodity, and
 - (ii) does not allow for cash settlement in place of delivery except where all or part of the delivery is rendered impossible or commercially unreasonable by an intervening event or occurrence not reasonably within the control of the counterparties, their affiliates, or their agents;
- (e) evidence of a deposit issued by a bank listed in Schedule I, II or III to the *Bank Act* (Canada), by an association to which the *Cooperative Credit Associations Act* (Canada) applies or by a person to which the *Trust and Loan Companies Act* (Canada) applies; or
- (f) evidence of a deposit issued by a loan corporation, trust corporation, credit union, caisse populaire, financial services cooperative or league that, in each

case, is authorized by an enactment of a jurisdiction of Canada to carry on business in a jurisdiction of Canada.

Note: For guidance regarding the types of derivatives described in this Regulation, see section 25 [Application] of Companion Policy 91-502CP *Trade Repositories and Derivatives Data Reporting*.

PART 3 EXCHANGE CONTRACTS

4. Proficiency

- (1) An advising representative or an associate advising representative of a portfolio manager must not act in that capacity in relation to exchange contracts unless the individual has
 - (a) earned a CFA Charter; or
 - (b) successfully completed the Derivatives Fundamentals Course and the Futures Licensing Course prepared and administered by CSI Global Education Inc. or any courses that preceded or succeeded those courses that do not have a significantly reduced scope and content when compared to the scope and content of the first mentioned courses.
- (2) If an individual is registered in a CMR Jurisdiction in the category of advising representative or associate advising representative on the CMR launch date, subsection (1) does not apply to the individual so long as the individual remains registered in that category.

5. Risk disclosure statement

- (1) A person registered as a dealer or adviser must deliver a written risk disclosure statement to a client before the person first
 - (a) purchases or sells an exchange contract for the client; or
 - (b) advises the client to purchase or sell an exchange contract.
- (2) The risk disclosure statement must be in
 - (a) the applicable IIROC form for the particular exchange contract product; or
 - (b) the risk disclosure form that would have been required by securities legislation to be delivered to the client with respect to the particular exchange contract product immediately before the coming into force of this section.

6. Registration exemption – International dealer

- (1) Subject to subsections (2) and (3), the dealer registration requirement does not apply to a person in respect of a trade in a non-Canadian exchange contract with a permitted client.
- (2) The exemption in subsection (1) is not available to a person unless all of the following apply:
 - (a) the head office or principal place of business of the person is in a designated foreign jurisdiction;
 - (b) the person is registered under the securities or derivatives legislation of the designated foreign jurisdiction in which its head office or principal place of business is located in a category of registration that permits it to carry on the activities in respect of exchange contracts in that jurisdiction that registration as a dealer would permit it to carry on in a CMR Jurisdiction;
 - (c) the person engages in the business of a dealer in exchange contracts in the designated foreign jurisdiction in which its head office or principal place of business is located;
 - (d) the person has submitted to the Chief Regulator a completed Form 91-501F1 *Submission to Jurisdiction and Appointment of Agent for Service*;
 - (e) the person does not maintain a physical place of business in Canada.
- (3) The exemption in subsection (1) is not available to a person in respect of a trade with a permitted client unless one of the following applies:
 - (a) the permitted client is a person registered under the securities legislation of a jurisdiction of Canada as an adviser or dealer;
 - (b) the person has notified the permitted client of all of the following:
 - (i) the person is not registered in the local jurisdiction to make the trade,
 - (ii) the foreign jurisdiction in which the head office or principal place of business of the person is located,
 - (iii) all or substantially all of the assets of the person may be situated outside of Canada,
 - (iv) there may be difficulty enforcing legal rights against the person because of the above,
 - (v) the name and address of the agent for service of process of the person in any CMR Jurisdiction.

- (4) The adviser registration requirement does not apply to a person that is exempt from the dealer registration requirement under this section if the person provides advice to a client and the advice is
 - (a) in connection with an activity or trade described in subsection (1); and
 - (b) not in respect of a managed account of the client.
- (5) A person that relied on the exemption in subsection (1) during the 12 month period preceding December 1 of a year must notify the Chief Regulator of that fact by December 1 of that year.
- (6) A person relying on the exemption in subsection (1) must
 - (a) file with the Chief Regulator a completed Form 91-501F2 *Notice of Regulatory Action* within 10 days of the date on which that person began relying on that exemption; and
 - (b) notify the Chief Regulator of any change to the information previously submitted under this subsection within 10 days of the change.
- (7) A person relying on the exemption in subsection (1) must deliver to the permitted client referred to in subsection (1), the risk disclosure, if any, that the person is required to provide to similar clients in the designated foreign jurisdiction in which its head office or principal place of business is located.

7. General condition to international dealer registration requirement exemption

The exemption in section 6 is not available to a person if the person is registered in a CMR Jurisdiction in a category of registration that permits the person to act as a dealer in an exchange contract for which the exemption is provided.

8. Registration exemption – International adviser

- (1) Subject to subsection (2), the adviser registration requirement does not apply to a person in respect of
 - (a) its acting as an adviser to a permitted client in respect of non-Canadian exchange contracts, other than a permitted client that is a person registered under the securities legislation of a jurisdiction of Canada as an adviser or dealer; or
 - (b) advising activities that are incidental to its providing advice on a non-Canadian exchange contract.
- (2) The exemption in subsection (1) is not available unless all of the following apply:
 - (a) the adviser's head office or principal place of business is in a designated foreign jurisdiction;

- (b) the adviser is registered in a category of registration, or operates under an exemption from registration, under the securities or derivatives legislation of the designated foreign jurisdiction in which its head office or principal place of business is located, that permits it to carry on the activities in respect of exchange contracts in that jurisdiction that registration as an adviser would permit it to carry on in a CMR Jurisdiction;
 - (c) the adviser engages in the business of an adviser in exchange contracts in the designated foreign jurisdiction in which its head office or principal place of business is located;
 - (d) as at the end of its most recently completed financial year, not more than 10 per cent of the aggregate consolidated gross revenue of the adviser, its affiliates and its affiliated partnerships was derived from the portfolio management activities of the adviser, its affiliates and its affiliated partnerships in Canada;
 - (e) before advising a client, the adviser notifies the client of all of the following:
 - (i) the adviser is not registered in the local jurisdiction to provide the advice described in subsection (1),
 - (ii) the designated foreign jurisdiction in which the adviser's head office or principal place of business is located,
 - (iii) all or substantially all of the adviser's assets may be situated outside of Canada,
 - (iv) there may be difficulty enforcing legal rights against the adviser because of the above,
 - (v) the name and address of the adviser's agent for service of process in any CMR Jurisdiction;
 - (f) the adviser has submitted to the Chief Regulator a completed Form 91-501F1 *Submission to Jurisdiction and Appointment of Agent for Service*.
- (3) A person that relied on the exemption in subsection (1) during the 12 month period preceding December 1 of a year must notify the Chief Regulator of that fact by December 1 of that year.
- (4) A person relying on the exemption in subsection (1) must
- (a) file with the Chief Regulator a completed Form 91-501F2 *Notice of Regulatory Action* within 10 days of the date on which that person began relying on that exemption; and
 - (b) notify the Chief Regulator of any change to the information previously submitted under this subsection within 10 days of the change.

- (5) A person relying on the exemption in subsection (1) must deliver to the permitted client referred to in subsection (1), the risk disclosure, if any, that the person is required to provide to similar clients in the designated foreign jurisdiction in which its head office or principal place of business is located.

9. General condition to international adviser registration requirement exemption

The exemption in section 8 is not available to a person if the person is registered in a CMR Jurisdiction in a category of registration that permits the person to act as an adviser in respect of the activities for which the exemption is provided.

PART 4 OVER-THE-COUNTER DERIVATIVES

10. Registration and prospectus exemptions

The registration requirement and the prospectus requirement do not apply in respect of a trade in an OTC derivative where each party to the trade is a permitted client or a qualified party, each acting as principal.

PART 5 STRIP BONDS

11. Removal of registration and prospectus exemptions

- (1) The exemptions from the dealer registration requirement contained in subsection 8.21(2) of National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* are not available for a trade in a strip bond.
- (2) The exemptions from the prospectus requirement contained in subsection 2.34(2) of National Instrument 45-106 *Prospectus Exemptions* are not available for a distribution of a strip bond.

12. Registration and prospectus exemptions

- (1) Subject to subsection (2), the dealer registration requirement and the prospectus requirement do not apply in respect of a trade in a strip bond.
- (2) The exemptions in subsection (1) are not available in respect of a trade made by a person to a purchaser that is a first-time purchaser, unless
- (a) if the person is not registered under the Act, the person provides the purchaser with an information statement before the purchaser enters into the trade and the purchaser acknowledges receipt of the information statement before the trade; or
 - (b) if the person is registered under the Act, the person provides the purchaser with an information statement before the purchaser enters into the trade.

- (3) The exemption from the dealer registration requirement in subsection (1) is not available to a person if the person is registered in a CMR Jurisdiction in a category of registration that permits the person to act as a dealer in a strip bond for which the exemption is provided.