The Bourse is recognized by the Autorité des marchés financiers [the “Autorité”] as an exchange and self-regulatory organization. The Regulatory Division [the “Division”] is a separate business unit of the Bourse responsible for carrying out the Bourse’s regulatory functions and operations. The Division consists of three units: examinations, market analyses and investigations, and regulatory and disciplinary affairs.

Last year, as part of its strategic planning, the Division initiated a reflection concerning its mission and vision. This exercise led the Division to a redefined mission and vision. The Division’s mission is to protect the integrity of the derivatives market and foster a compliance culture in collaboration with the various stakeholders. To this end, its vision is to carry out regulatory activities in an efficient and transparent manner by focusing on innovation and considering market challenges.

The Division is pleased to issue its first newsletter for the period of July 1 to December 31, 2017, including a summary of 2017. The Division intends to issue a bi-annual newsletter to share information of a general nature on regulatory activities and to use this opportunity to share observed best practices in regulatory compliance.

Enjoy!

**Topics**

**Profile of approved participants and persons**
- Approved participants
- Approved persons

**Regulatory activities**
- Examinations
- Special inspection on LOPR
- Market analyses and investigations
- Disciplinary proceedings
- Imposition of late filing fees

**Observed best practices in supervision and compliance**

**Coming events organized by the Division**
Profile of approved participants and persons

Approved participants

As of December 31, 2017, the Bourse had a total of 73 approved participants that were geographically distributed as follows:

Figure 1

Geographical Distribution of Bourse de Montréal’s Approved Participants

Approved persons

For the period of July 1 to December 31, 2017, the Division processed 70 applications for approval as approved persons, generating a total of 143 requests in 2017. As of December 31, 2017, the Bourse had 770 approved persons distributed as follows: 62 in the United Kingdom, 344 in the U.S., 362 in Canada and 2 in Israel.

Figure 2

Geographical Distribution of Bourse de Montréal’s Approved Persons
Regulatory activities

Examinations

The Examinations Unit reviews the derivative instrument trading desks of the approved participants of the Bourse. These examinations are used to verify whether the approved participants’ trading practices comply with the Rules and Policies of the Bourse. The reviews include:

- Audits, of a sample of orders entered into the Bourse’s automated trading system and the transactions executed therein;
- Reviews of current procedures as well as their relevance and completeness;
- Audits of various books and records.

Once the review is complete, a report is issued summarizing any deficiencies found during the review and establishing requirements and recommendations for correcting the observed deficiencies. The report is issued to the attention of the approved participant.

From July 1 to December 31, 2017, the Division performed 15 examinations. The most frequent findings in these examinations were:

- Failure to provide the Bourse with a unique identifier for each client with direct electronic access (see article 6366 and Circular 083-17).
- Identification of incorrect orders, such that certain account type markers did not reflect the true beneficiary of the account (see article 6376).
- Failure to include all the accounts with positions that should be reported in a LOPR or to attribute the appropriate beneficiary for several accounts with positions that should be reported (see the Regulatory Requirements Guide - LOPR).
- Employees of approved participants who were not persons approved by the Bourse had access to the trading system (see article 6366).

In 2017, the Division performed a total of 27 examinations and 1 pre-examination that led to findings.

Special inspection on LOPR

On September 1, 2017, the Division issued a circular (Circular 124-17) providing approved participants with: (1) supplementary regulatory guidance on requirements with respect to their LOPR reports and the related surveillance and compliance system, and (2) notification of the special inspection on LOPR.

Following this publication, the Division communicated with each of the participants targeted by the special inspection on LOPR. The Division asked each participant to review the contents of its LOPR reports and certify that, as of August 31, 2017: (i) its reports complied with the regulatory requirements of the Bourse, and (ii) that it had met the surveillance and compliance requirements regarding LOPR reports by implementing a system “that is reasonably designed to achieve compliance.” The participants sent this certification to the Division on or before November 1, 2017.

The special inspection targeted 65 approved participants (30 Canadian participants and 35 foreign participants). The Division received no requests from participants for a postponement.
Seven of the eight participants that filed a notice of non-compliance included an action plan describing the corrective measures to be taken. The Division has followed up and will continue to follow up with these participants to ensure that they carry out the action plans submitted.

The Division received no notices of non-compliance reporting a critical situation. Rather, the participants appear to have used the opportunity afforded by the special inspection to improve their processes or correct some of the noted shortcomings.

Lastly, late fees (for late filing) were imposed on participants that were late in filing their certification or notice of non-compliance. Late fees in a total amount of $7,250 were imposed.

These late fees were imposed on late filers out of consideration for participants that had complied with the prescribed times during the special inspection.

**Market analyses and investigations**

The Market Analysis unit performs market surveillance to detect potential breaches of regulations and monitors insider trading on the options market of the Bourse. The Market Analysis unit also reviews trading on the derivative products markets to determine whether participants are complying with trading rules and principles and whether these trades involve abusive or manipulative trading practices.

From July 1 to December 31, 2017, the Division monitored over 6,760,900 trades executed on the Bourse.

The Market Analysis unit is also responsible for conducting a preliminary review of all the complaints received, from various sources. The Division received two complaints in the period from July 1 to December 31, 2017: one from a client and another from an approved participant. An investigation was opened concerning one of these complaints.
The Investigations unit may open an investigation once a potential regulatory violation has been detected during an examination or following a market analysis.

From July 1 to December 31, 2017, the Division opened three investigations, concerning in particular access to the trading system of the Bourse by employees of participants, when those employees were not approved persons, as well as exchange-for-related-positions transactions. During this same period, the Division completed five investigations.

Disciplinary proceedings

Disciplinary proceedings may be initiated when, following an investigation, the Division concludes that there has been an offence to the Rules of the Bourse or to regulations (for example, Regulation 23-103).

Disciplinary complaints

In 2017, two disciplinary decisions were rendered, giving effect to settlement offers concerning participants’ failure to have obtained prior approval from the Bourse before allowing some of its employees to access the electronic trading system, as well as participants’ failure to fulfill their obligation to establish and maintain a system for supervising the activities of each of its employees that is reasonably designed to achieve compliance with the Rules and Policies of the Bourse (Circular 012-17 and Circular 051-17).

Figure 6
Fees and Fines Imposed as Part of Disciplinary Matters

Fines for minor violations

On May 10, 2017, the Bourse de Montréal self-certified a regulatory amendment implementing a process to impose fines for minor violations. This process, introduced by articles 4220 to 4224 of the Rules of the Bourse, is an alternative enforcement process. The violations targeted by this process are not qualified as “minor.” Only the circumstances leading to the commission of a violation as listed in article 4220 can be considered “minor” and, as such, justify a decision from the Vice-President of the Regulatory Division to opt for the imposition of a fine instead of the filing a disciplinary complaint.
The Division also used the process to impose fines for minor violations in three disciplinary matters. Two of these matters were closed following non-contestation of the notices of violations by the participants involved and the issuance and serving of notices of fines for the minor violations committed. As for the third matter, the participant involved with the notice of minor violation submitted written observations and additional evidence. Following an analysis of this additional evidence, a notice was issued and served advising that the matter had been closed. The violations for these files consisted of having failed to advise the Division that position limits had been exceeded and having failed to submit a notice of non-compliance under article 4002. No fine was imposed since, in the case of the issuance of the notice of violation, it was a first occurrence.

To recap, in 2017, 5 disciplinary matters were concluded. For 3 of them, the Division used the process to impose fines for minor violations, for the other 2, offers of settlement were established following the filing of disciplinary complaints.

For all disciplinary matters settled in 2017, participants paid fines in a total amount of $85,000 and expense refunds in an amount of $9,750. These amounts were received by the Division and deposited into the Fines Fund.

### Imposition of late fees

The following table provides detailed information on all the fees imposed by the Division from July 1 to December 31, 2017 for late production of documents:

<table>
<thead>
<tr>
<th>Fees imposed</th>
<th>Number of occurrences</th>
<th>Number of participants</th>
<th>Total amount imposed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Termination notice submitted more than 10 days</td>
<td>7</td>
<td>5</td>
<td>$15,000</td>
</tr>
<tr>
<td>after the termination date</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Late reporting of corporate amendments</td>
<td>0</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Report pertaining to the accumulation of positions</td>
<td>26</td>
<td>20</td>
<td>$17,750</td>
</tr>
<tr>
<td>for derivative instruments (LOPR)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Semi-monthly reports for over-the-counter options</td>
<td>0</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>(Rule Nine)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Information or document required by the Division</td>
<td>0</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>
Observed best practices in supervision and compliance

Each approved participant must, at the time of its approval and as long as it remains approved, establish and maintain a system to supervise the activities of each employee, agent of the approved participant and client, that is reasonably designed to achieve compliance with the Rules and Policies of the Bourse and with any legislation and regulations applicable to securities and derivative instrument activities.

These supervision and compliance obligations are based on principles; no single approach applies to all participants. As a result, it is up to participants to design and implement a supervision system that will be tailored to their business model, structure and risks.

The Division acknowledges that it must allow participants the latitude to determine what is appropriate based on their needs and adjust their systems accordingly. In order to provide participants with guidance in the design of their supervisory system and in their assessment of its reasonableness, on September 13, 2017, the Division published Guidelines on Supervision and Compliance Obligations (Circular 128-17).

Furthermore, the Division has observed the following best practices concerning supervision and compliance obligations:

• Policies and procedures appear to be better understood by the participant’s employees when, in addition to containing references to the applicable rules, they explain the requirements in other terms, describe the required tasks, and contain examples from the participant’s structure, organization and environment;
• A clear delegation of tasks and responsibilities generally results in better processes and higher-quality audit trails;
• Tasks and responsibilities should be consistent with the participant’s policies and procedures;
• Regular reviews of policies and procedures should be conducted to ensure that all regulatory changes have been immediately incorporated;
• A pre-production review should be conducted of the parameters and controls in place for all the participant’s employees and not only its clients;
• A review of alerts and their parameters should be conducted to ensure that they are still appropriate;
• A clear escalation process should be in place, including audit trails for the steps taken by the participant.

Coming events organized by the Division

Parlons Dérivés (Montréal) / Derivatives Exchange (Toronto) conference:
June 2018 – dates to be confirmed