

13.3.2 Notice and Request for Comment – Application by The London Metal Exchange for Exemption from Recognition and Registration as an Exchange and Related Registration Relief

NOTICE AND REQUEST FOR COMMENT

APPLICATION BY
THE LONDON METAL EXCHANGE FOR
EXEMPTION FROM RECOGNITION AND REGISTRATION AS
AN EXCHANGE AND RELATED REGISTRATION RELIEF

A. Background

The London Metal Exchange (**LME**) has applied to the Commission for an exemption from the requirement to be registered as an exchange pursuant to section 15 of the *Commodity Futures Act* (Ontario) (**CFA**), and the requirement to be recognized as an exchange pursuant to section 21 of the *Securities Act* (Ontario) (**OSA**).

LME is regulated as a Recognised Investment Exchange (**RIE**) by the UK Financial Conduct Authority (**FCA**), pursuant to the UK *Financial Services and Markets Act 2000* (**FSMA**). As a RIE, LME facilitates the trading in futures and options contracts in base and precious metals (**LME Contracts**).

LME proposes to offer direct access in Ontario to its trading facilities to prospective participants in Ontario (**Ontario Participants**).

As LME will be carrying on business in Ontario, it is required to be recognized as an exchange under the OSA and registered as a commodity futures exchange under the CFA or apply for exemptions from both requirements. LME has applied for an exemption from the registration and recognition requirements on the basis that it is already subject to regulatory oversight by the FCA.

B. Related Relief

LME intends to provide direct access to its trading facilities to Ontario Participants who will be certain Canadian financial institutions and certain other market participants that have a head office or principal place of business in Ontario, such as banks listed in Schedule I of the *Bank Act* (Canada) (**Banks**).

LME is requesting exemptive relief from the registration requirements under section 22 of the CFA for trades in LME Contracts by Ontario Participants, including Banks entering orders as principal and for only their own account, and “hedgers”, as defined in subsection 1(1) of the CFA (**Hedgers**).

C. Application and Draft Exemption Order

In the application, LME has outlined how it meets the criteria for exemption from recognition and from registration. The specific criteria can be found in Appendix 1 of the draft exemption order. Subject to comments received, Staff intends to recommend that the Commission grant an exemption order with terms and conditions based on the draft exemption order. The application and draft exemption order are attached as Appendices A and B, respectively, to this Notice.

D. Comment Process

The Commission is publishing for public comment LME’s application and the draft exemption order. We are seeking comment on all aspects of the application and draft exemption order.

Please provide your comments in writing, via e-mail, on or before **December 7, 2018**, to the attention of:

Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, Ontario M5H 3S8
Fax: 416-593-2318
Email: comments@osc.gov.on.ca

The confidentiality of submissions cannot be maintained as the comment letters and a summary of written comments received during the comment period will be published.

Questions may be referred to:

Christopher Byers
Senior Legal Counsel, Market Regulation
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Alina Bazavan
Senior Analyst, Market Regulation
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APPENDIX A



5 October 2018

Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, ON M5H 3S8

Attention: Secretary to the Commission

Dear Sirs/Mesdames:

RE: The London Metal Exchange Application for Exemption from Recognition as an Exchange and Registration as a Commodity Futures Exchange

We are filing this application with the Ontario Securities Commission (**OSC**) for the following decisions (collectively, the **Requested Relief**):

1. An order under Section 147 of the *Securities Act* (Ontario) (**OSA**) exempting London Metal Exchange (the **Exchange** or the **LME**) from the requirement to be recognized as an exchange under Section 21(1) of the OSA (the **OSA Relief**);
2. An order under Section 80 of the *Commodity Futures Act* (Ontario) (CFA) exempting the LME from the requirement to be registered as a commodity futures exchange under Section 15(1) of the CFA (together with the OSA Relief, the **Exchange Relief**);
3. An order under Section 38 of the CFA exempting trades in contracts on the LME by a “hedger”, as defined in subsection 1(1) of the CFA (**Hedger Relief**) from the registration requirements under Section 22 of the CFA (**Hedger Relief**); and
4. an order under Section 38 of the CFA exempting trades in contracts on the LME by a bank listed in Schedule I to the *Bank Act* (Canada) (**Bank**) entering orders as principal and for its own account only from the registration requirement under Section 22 of the CFA (**Bank Relief** and, together with the Hedger Relief, **Registration Relief**).

OSC Staff has prescribed criteria in OSC Staff Notice 21-702 *Regulatory Approach for Foreign Based Stock Exchanges*, as updated, (**Staff Notice 21-702**) in relation to applications by foreign exchanges for an exemption from the exchange recognition requirement and for applications by foreign-based commodity futures exchanges for an exemption from the exchange registration requirement. These criteria are set out in Appendix A to the attached draft order.

Reference will be made in this application to the LME Rules and Regulations and Appendices thereto (the **LME Rules**) which can be found at:

<https://www.lme.com/About/Regulation/Rules/Rulebook>

For convenience, this Application is divided into the following Parts:

Part I Background

Part II Application of Approval Criteria to the Exchange

1. Regulation of the Exchange
2. Governance
3. Regulation of Products
4. Access
5. Regulation of Participants on the Exchange
6. Rulemaking
7. Due Process
8. Clearing and Settlement
9. Systems and Technology

10. Financial Viability
11. Transparency
12. Record Keeping
13. Outsourcing
14. Fees
15. Information Sharing and Oversight Arrangements
16. IOSCO Principles

Part III Submissions

Part IV Other Matters

Part I Background

Description of the LME and its business

1. The LME is a private company registered in England and Wales (registered number 2128666) whose registered office is at 10 Finsbury Square, London, EC2A 1AJ, United Kingdom (**UK**).
2. The LME is the world centre for industrial metals trading and price-risk management. The majority of all global non-ferrous trading business is conducted on the LME and the prices discovered on the Exchange's three trading platforms are used as global reference prices. In 2017 this equated to US \$12.7 trillion notional, 3.5 billion tonnes of metal and over 157 million lots.
3. The primary functions of the Exchange are to:
 - (a) provide a market where participants have the opportunity to hedge against risk arising from price fluctuations in metals;
 - (b) determine reference prices for the worldwide pricing of trades relating to non-ferrous base metals and steel; and
 - (c) regulate appropriately located storage facilities to enable market participants to make or take physical delivery of approved metal brands, which are traded on the Exchange.
4. LME operates and regulates a trusted financial market where there is always a buyer and a seller, where there is always a price and where there is always the opportunity to transfer or assume exposure to a risk. The LME does not conduct any trading on its own account.
5. Founded in 1877, the LME operates futures and options markets in thirteen industrial, base metals. Copper and tin have been traded on the Exchange since 1877; lead was introduced in 1903, zinc in 1915, primary aluminium in 1978 and nickel in 1979. The two grades of aluminium alloy (aluminium alloy for Europe and NASAAC for North America) were introduced in 1992 and 2002 respectively. In 2008, the LME launched two regional contracts for steel billet; in July 2010, these contracts merged into a single global contract. Cobalt and Molybdenum were launched in 2010. Ferrous metal contracts in cash settled steel scrap, cash settled steel rebar and four regional aluminium premium contracts, were launched in 2015. The most recent contracts are loco London precious metals contracts, LME Gold and LME Silver futures launched in 2017.
6. The LME may technically be described as an on-exchange forwards market. LME contracts are based on physical settlement by the transfer of ownership of metal stored in listed warehouses; this guarantees price convergence as the far futures settlement dates converge on the cash settlement date (i.e. two days forward). The ability to make or take delivery of metal against an LME futures contract on the settlement date acts to prevent any divergence between LME settlement price and the physical metal price.
7. Trading on the LME can take place on any one of the following three venues.
 - (a) Open Outcry: The LME trading floor (known as the **Ring**) is located in London. Ring trading is conducted by open outcry, during specified morning and afternoon sessions.
 - (b) Inter-Office Market: Inter-office trading is the bi-lateral trading of LME contracts, usually by telephone. Unlike ring trading, it can take place 24 hours a day. While only Cleared Contracts are traded in the Ring, both Cleared Contracts and Client Contracts are traded inter-office. Like ring trading, inter-office trading takes place on a 'quote driven' basis, with dealers providing bids and offers over the phone.

- (c) LMEselect: Category 1 and Category 2 Members¹ who have specific permission from LME may trade Cleared Contracts via LME's electronic trading system (**LMEselect**). It is expected that certain of LME's Members will wish to trade via LMEselect through persons who are physically located in Ontario² and that certain Ontario incorporated entities may wish to become Members of the LME.
8. Settlement of LME futures contracts is determined first by offsetting the positions of Members and then by delivery of LME warrants to balance the trading activities of the Members. This takes place on the settlement date such that ownership of the underlying metal changes hands on the day; there is no settlement window. The offset mechanism allows the Members who trade on the LME to reduce the number of LME warrants that are transferred in order to settle their obligations on a settlement day. For example a producer who hedges its risk to a drop in metal prices will sell for delivery on a future date on the LME. It will close out its hedge by buying back an equal amount of metal for delivery on the same date on the LME. The metal delivery obligations will offset exactly and result in no LME warrants changing hands but the price differences will produce a net cash payment on that date.
9. An LME warrant is a bearer document that represents the ownership of a specific number of tonnes of an identified brand of metal, stored in an identified shed (facility in a particular warehouse) operated by an LME approved warehouse company. The LME oversees and controls metal brand listing and warehouse approval because the quality and availability of metal stored in LME approved warehouses underpins the integrity of trading and price discovery.
10. The LME proposes to offer access its trading services and clearing services to prospective participants in Ontario. In order to obtain direct access to the Exchange, a prospective member in Ontario must execute a membership agreement in which the prospective member agrees to abide by the LME Rules and consent to submit to the jurisdiction of the Exchange. Prospective members and other participants in Ontario who are currently or will in the future be admitted by LME (**Ontario Participants**) may access the LME via LMEselect and the Inter-Office Market from Ontario, and may also apply to become ring-dealing Members if they wish. The LME Rules provide clear and transparent access criteria and requirements for all LME market participants, as well as minimum financial requirements for participants to maintain the financial integrity of the Exchange. The LME applies these criteria to all LME participants in an impartial manner.

Descriptions of categories of LME membership

11. LME has seven membership categories and each member category has different associated capabilities, obligations and responsibilities. Only Categories 1 to 4 have any trading rights and are eligible to have direct access to LMEselect. A summary of the membership categories is set out below:
- (a) Category 1: These members have the exclusive right to trade Cleared Contracts by open outcry in the Ring, on the telephone (i.e. inter-office) market and on LMEselect and are entitled to issue Client Contracts to their clients. As Clearing Members, they are permitted to clear trades on their own behalf and on behalf of their clients and, as a result, must be members of LME Clear. Category 1 Members must be regulated by the Financial Conduct Authority (**FCA**).
- (b) Category 2: These members are Clearing Members and are permitted to trade Cleared Contracts in the telephone market and on LMEselect and issue Client Contracts. As Clearing Members, they are permitted to clear trades on their behalf and on behalf of their customers and, as a result, must be members of LME Clear. Category 2 members must be regulated by the FCA, a competent authority of an EEA State or benefit from an exclusion under the Financial Services and Markets Act 2000 (Regulated Activities) Order (**RAO**) Article 72 such as qualifying as an Overseas Person i.e. an Unauthorised Overseas Participant.
- (c) Category 3: These members are Clearing Members and are permitted to trade Cleared Contracts in the telephone market and on LMEselect but are not permitted to issue Client Contracts, being proprietary traders. As Clearing Members, they are permitted to clear trades on their own behalf only and, as a result, must be members of LME Clear. Category 3 Members must be regulated by the FCA, a competent authority in an EEA state, or benefit from an exclusion under the RAO.
- (d) Category 4: These members are not Clearing Members and must appoint a designated Clearing Member to clear trades on their behalf. These members are permitted to trade Client Contracts in the telephone market and on LMEselect and are permitted to issue Client Contracts. Category 4 members may either be regulated by the FCA, a competent authority in an EEA State or benefit from an exclusion under the RAO such as qualifying as an Unauthorised Overseas Participant.

¹ See section 11 for a description of the member categories.

² Such persons may be employed by the Member itself or may be employed by an affiliate, but all trading is carried out in the name of the Member.

- (e) Category 5: These members are customers of Category 1, 2 or 4 Members in that they receive Client Contracts but are not permitted to issue them. Category 5 members are not required to be regulated.
- (f) Category 6: Individual members are persons who wish to maintain links with the Exchange for business purposes, such as consultants and arbitrators. These members have no trading rights on LME.
- (g) Category 7: Honorary membership is conferred on individuals who have given conspicuous service to the LME at the discretion of the Exchange, e.g. former chief executives and chairmen of the LME. These members have no trading rights on the LME.

Ontario Participants and Requested Relief

- 12. The LME currently expects that Ontario Participants will be comprised of banks listed in Schedule 1 of the Bank Act (Canada) (**Ontario Banks**). The LME also services the physical market and other entities, such as industrial hedgers, may wish to join in the future.
- 13. LME intends to provide Ontario Participants with direct access to the LME. LME is requesting the Registration Relief and the Hedger Relief in order for Ontario Participants to be able to access trading on the LME directly, without having to be registered as dealers under the CFA in the case of the Registration Relief.

Location

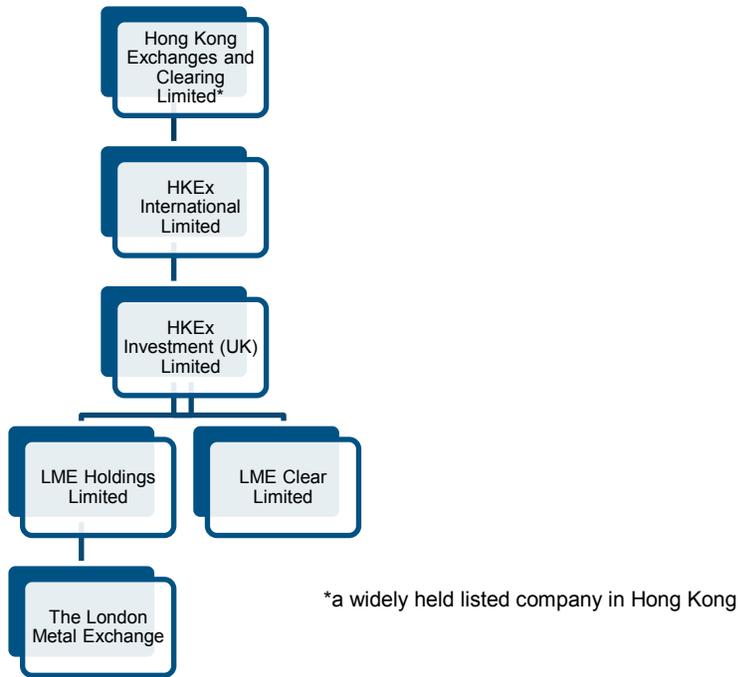
- 14. LME is based in London, England. It also had a representative office in Singapore which opened in 2010. Singapore limits the amount of time a representative office may be open. Accordingly, this office became a branch office on October 15, 2012.

Size

- 15. The LME is a highly liquid market and in 2017 achieved traded volumes of over 157 million lots, equivalent in value to US\$12.7 trillion notional. The LME is a global market with an international membership. More than 575 brands of metal from over 60 countries are approved as “good delivery” against LME contracts. There are over 550 LME approved warehouses in 14 countries and 34 locations globally.

Ownership and corporate structure

- 16. The LME is a wholly-owned subsidiary of LME Holdings Limited, a private limited company registered in England and Wales (registered number 4081218). LME Holdings Limited has no trading subsidiaries other than the LME. The LME has no subsidiaries.
- 17. LME Holdings Limited (the sole shareholder of LME) in turn is a wholly owned subsidiary of HKEx Investment (UK) Limited, which is a wholly owned subsidiary of HKEx International Limited (a private limited company) registered in Hong Kong. HKEx International Limited is wholly owned by Hong Kong Exchanges and Clearing Limited (**HKEX Group**), a publicly listed company registered in Hong Kong and listed on the Hong Kong stock exchange. The LME is managed by a board comprising independent directors, additional directors and LME’s Chief Executive Officer. Please see the organizational chart attached as Annex 1.
- 18. The following is a diagram of the chain of ownership of the LME and its affiliated clearing house, LME Clear Limited (**LME Clear**):



LME Clear

19. LME Clear was established to act as the central counterparty (**CCP**) in relation to all classes of contracts that are traded on the LME. LME Clear is an approved CCP under the European Market Infrastructure Regulation (**EMIR**) and is supervised by the Bank of England (the **Bank**) in the UK. LME Clear is also applying to the OSC for an exemption at this time.

Products traded on the Exchange

20. Futures contracts are contracts for delivery of a particular metal on a specified date (Prompt Date) of a prescribed quantity of metal, the specification for which is in accordance with LME's special contract rules (covering quality of material, its shape and weight, the size of each lot and the currency in which the price is quoted). The lot size for primary aluminium, copper, zinc and lead is 25 tonnes; for aluminium alloy and NASAAC, it is 20 tonnes; for nickel is 6 tonnes; for tin is 5 tonnes; for steel billet is 65 tonnes; for cobalt is 1 tonne; and for molybdenum is 6 tonnes. Futures contracts for metals are deliverable for all London business days out to 3 months (i.e. daily settlement). Other Prompt Dates at less frequent intervals are available out to 27 months and beyond this for certain metals up to a maximum of 10 years.
21. LME offers trading in futures contracts in the eleven metals listed in paragraph 5 above. In addition, LME offers:
 - (a) traded options contracts which give the right to buy or sell the underlying futures contracts for primary aluminium, copper, zinc, lead, nickel, tin, NASAAC, aluminium alloy and LMEX (see (iii) below) until a specified date in the future;
 - (b) contracts known as Traded Average Price Options which provide a hedging tool for participants in the metals industry that price contracts on the basis of a monthly average price;
 - (c) a contract known as the LMEX which is an index contract based on a basket of metals (this has not traded for a number of years but remains available to trade);
 - (d) mini-contracts in primary aluminium, copper and zinc;
 - (e) contracts known as Monthly Average Futures which are monthly average price futures contracts and are available for primary aluminium, aluminium alloy, copper, zinc, lead, nickel, NASAAC and tin; and

- (f) daily and monthly futures contracts for both gold and silver, known as LMEprecious.
22. Traded options contracts give the right to buy or sell the underlying futures contracts for all LME metals. They are traditional 'American' style options (options that may be exercised on any day in its life) and can be purchased against a short or long futures contract.
23. Traded Average Price Options provide a hedging tool for participants in the metals industry that price contracts on the basis of a monthly average price. Traded Average Price Options are 'Asian' style options (options exercised at the average underlying price over a period) giving the right to buy or the right to sell metal at the average LME price for a given month.
24. The LMEX is an index contract based on the index weighted values of copper, primary aluminium, zinc, nickel, tin and lead, as traded on the LME. Only futures are available on the index as options were suspended in April 2013.
25. LMEminis are smaller contracts traded in lots of five. Unlike other LME products, the LMEX and LMEminis are cash cleared.
26. Monthly Average Futures are monthly futures contracts settled in cash against the monthly average of the daily cash settlement price of the relevant metal during the relevant month. The amount payable on maturity is the difference between the 'fixed' price agreed at the time of the contract and the average price for the relevant month.

LME Contracts

27. All LME contracts (i.e. contracts under which metal is traded in accordance with the LME Rules) are entered into on a principal to principal basis. Regulation 1.4 of Part 3 of the LME Rules specifies that LME contracts may only be written by a Category 1 Member, Category 2 Member or Category 4 Member (each of which are brokers regulated by the FCA), the effect of which being that all LME contracts will have at least one party being a Member of LME. Members who enter into LME contracts therefore deal off their own book, entering into an equivalent contract with customers for whom they are acting. In addition, the Members will typically have entered into a separate contractual arrangement with their customers setting out the basis on which trades will be executed on the instructions of customers.
28. LME contracts take one of two forms: Cleared Contracts and Client Contracts. Participants located in Ontario will be able to be trade through LMEselect and access the Inter-office market and trade on the Ring³ (provided that the relevant membership requirements are met).
29. LME operates an open offer model under which Contingent Agreements to Trade on the exchange result in Cleared Contracts at the CCP. These terms are defined in the LME Rules. Cleared Contracts are contracts between LME Clear, as the CCP, and the buyer and seller, as the case may be. There will be no initial contract between the trading parties. Instead LME Clear makes an offer to each party to the trade: it will offer to act as the buyer to the party who wishes to be the seller, and it will offer to act as the seller to the party who wishes to be the buyer.
30. Client Contracts are contracts between a Member entitled to handle customer business and its customers. These contracts are not made with LME Clear and therefore the contractual obligations remain with the original parties. Members are required to enter details into the LME's matching system (**LMESmart**) and contracts arise between either the Clearing Member and the CCP or the Member and the Client. However Clearing Members are not obliged to enter into a trade with another Clearing Member to "back off" the Client Contract. Failure to enter trades into matching could result in disciplinary action by the LME.
31. The LME Rules provide that any dispute as to the existence, completion or validity of any LME contract, as well as any dispute arising out of such a contract, will be referred to arbitration proceedings administered by LME. Parties entering into LME contracts are deemed to waive any immunity from suit or arbitration or the execution of any judgment or award on the ground of sovereignty, nationality, domicile, residence or otherwise.

³ Given that Ring trading takes place physically in London on the LME trading floor, the only way that an Ontario participant could take part in Ring trading would be if an Ontario-incorporated entity established a London presence and became a Category 1 member.

Part II Application of Approval Criteria to the Exchange

1 REGULATION OF THE LME

1.1 Regulation of the Exchange – The exchange is regulated in an appropriate manner in another jurisdiction by a foreign regulator (the Foreign Regulator).

1.1.1 The LME is subject to a comprehensive regulatory regime in the UK and Europe and is a Recognised Investment Exchange (**RIE**) regulated by the Financial Conduct Authority (**FCA**). This regulatory structure includes: financial and other fitness criteria for Members of LME; reporting and record-keeping requirements; procedures governing the treatment of customer funds and property; conduct of business standards; provisions designed to protect the integrity of the markets; and statutory prohibitions on fraud, abuse and market manipulation.

1.1.2 Responsibility for financial services legislation and broad policy in the UK lies with Her Majesty's Treasury, which is answerable to UK's Parliament. Responsibility for regulating the conduct of investment business, providing investor protection and preventing market manipulation in the UK rests with the FCA, the successor to the Financial Services Authority (**FSA**) which became responsible for the supervision of UK RIEs on April 1, 2013 as part of the UK's program of regulatory reform. Additional authority rests with the UK's Department for Business, Energy and Industrial Strategy which is responsible for modernising company law and reforming corporate governance and investigates the conduct of companies and the Serious Fraud Office, which investigates and prosecutes serious and complex fraud, bribery and corruption and so maintains confidence in the probity of business and financial services in the UK. The Prudential Regulatory Authority, created as a part of the Bank by the *Financial Services Act 2012*, is responsible for the prudential regulation and supervision of around 1,700 banks, building societies, credit unions, insurers and major investment firms. It does not have authority in relation to RIEs.

1.1.3 The principal legal provisions for investor protection in the UK's financial services sector are contained in, or derived from, the UK *Financial Services and Markets Act 2000 (FSMA)* and the FCA fulfils its regulatory responsibilities within the framework established by FSMA and related legislation.

1.1.4 The FCA is an independent non-governmental body, given statutory powers by FSMA. It is a company limited by guarantee (registered in England and Wales with number 1920623) whose registered office is at 12 Endeavour Square, London, England, E20 1JN.

1.1.5 As a non-governmental body, the FCA is operationally independent of government. It is accountable to the ministers within Her Majesty's Treasury and through the Ministers in this department, to UK's Parliament. It is also subject to the scrutiny of the National Audit Office, Treasury Select Committee and Parliamentary Accounts Committee.

1.1.6 The board of the FCA sets its overall policy. Board members are appointed by the Treasury. The majority of the board members are non-executive. The non-executive directors check that the FCA operates efficiently and economically. They oversee the FCA's mechanisms of financial control and set the pay of the executive members of the board.

1.1.7 General strategic and policy matter decisions are taken by the FCA board and/or its Executive Committee. Other major regulatory decisions (including appeals in respect of disciplinary matters and warning) are taken, on behalf of the FCA board, by the Regulatory Decisions Committee which comprises current and recently retired practitioners and non-practitioners, all of whom represent the public interest.

1.1.8 The FCA has an objective to promote effective competition in consumers' interests in regulated financial services. In addition to this, the organisation also has a competition duty. In April 2015, the FCA were given concurrent powers to enforce against breaches of competition law, alongside the Competition and Markets Authority for the provision of financial services generally.

1.1.9 The FCA is an independent body which does not receive any funding from Her Majesty's Government. To finance its work, the FCA charges fees to the entities that it regulates, including the LME.

1.1.10 The general powers of the FCA to raise these fees are set out in Schedule 1, Part III, paragraph 17 of FSMA. FSMA also gives the FCA the power to maintain sufficient reserves. In the latest annual report of the FCA, anticipated funding for 2017/18 is £508m as set out in the FCA's Business Plan a copy of which can be found at:

<https://www.fca.org.uk/publications/corporate-documents/our-business-plan-2017-18>.

1.1.11 The FCA currently has staff costs of £316.8m rising to £324.2 for 2017/18. Staffing represents the highest cost to the FCA.

- 1.2 **Authority of the Foreign Regulator – The Foreign Regulator has the appropriate authority and procedures for oversight of the exchange. This includes regular, periodic oversight reviews of the exchange by the Foreign Regulator.**

Scope of authority

- 1.2.1 The FCA has three specific, and equal, operational objectives set by UK's Parliament. These are to: secure an appropriate degree of protection for consumers; protect and enhance the integrity of the UK financial system; and promote effective competition in the interests of consumers. In practice, this means that the FCA wants to make markets work effectively to deliver benefits to firms and consumers.
- 1.2.2 The FCA regulates some 73,000 businesses. The firms range from global investment banks to very small businesses. It operates a risk-based approach concentrating on the significant risks and accepting that some failure neither can, nor should, be avoided. Potential risks are prioritized, using an impact and probability analysis, and the FCA will then decide on an appropriate regulatory response – in other words, what approach it should take and what resources it will allocate to mitigating risk.
- 1.2.3 The FCA's risk-based regulatory approach to the supervision of exchanges includes regular risk assessments designed to identify the main risks to its statutory objectives as they arise and to help it plan how to address these risks. This process involves drawing on a wide range of sources. The FCA uses this information to assess the level of risk posed to its statutory objectives and to decide on what approach is needed (if any) to mitigate risk.

Authorizing statutes

- 1.2.4 The FCA was created by the *Financial Services Act 2012* which amended FSMA, the primary piece of legislation from which it derives its powers and functions. Rules and guidance made in the FCA Sourcebook for Recognised Investment Exchanges (**REC**) are made pursuant to powers granted under FSMA.
- 1.2.5 Her Majesty's Treasury has the power to enact secondary legislation under FSMA, which affects the way the FCA operates. The most important piece of secondary legislation is the Financial Services and Markets Act (Regulated Activities) Order 2001 (**RAO**). The RAO sets out the specific activities for which firms must receive FCA permission (known as a Part IV permission) to carry on investment business, or where they can avail themselves of an exemption or exclusion, as the case may be.
- 1.2.6 The FCA is the designated competent authority under the European single market directives for banking, insurance, investment business, payment services, collective investment schemes and other financial services, including insurance intermediation. It is also the competent authority under many other EU directives, including the Market Abuse and Prospectus Directives. As a result, it is the UK representative within the relevant EU regulatory bodies such as the European Securities and Markets Authority. European legislation affecting the FCA in regulated financial services is implemented through the FCA Handbook and/or Her Majesty's Treasury regulations.
- 1.2.7 Other main areas of FCA regulation include personal pension schemes and activities relating to regulated mortgage contracts. It has authorisation, enforcement, supervision and rule-making functions for firms (some prudential supervision is now undertaken by a subsidiary of the Bank, the Prudential Regulation Authority (**PRA**)). It also has registration functions under the various legislation applicable to mutual societies and related functions under other legislation applicable to financial services and listing. FSMA also provides the FCA with powers over unregulated firms and persons regarding market abuse, breaches of money laundering regulations and short selling. The FCA also has the power to prosecute unauthorized firms or persons carrying on regulated activities.

Source of its authority to supervise the foreign exchange

- 1.2.8 LME is an RIE in accordance with section 285 of FSMA. As an RIE, LME is exempt from the general prohibition in respect of any "regulated activity" which is carried on as part of LME's business as an investment exchange.
- 1.2.9 To acquire and maintain recognition status as an RIE, LME must satisfy several statutorily-prescribed recognition requirements set out in the Financial Services and Markets Act 2000 (FSMA Recognition Requirements for Investment Exchanges and Clearing Houses) Regulations 2001 (SI 2001/995) as amended by the Financial Services and Markets Act 2000 (FSMA Recognition Requirements for Investment Exchanges and Clearing Houses) (Amendment) (Regulations) 2006 (the **FSMA Recognition Requirements**). The FSMA Recognition Requirements for RIEs can be found at: <https://www.handbook.fca.org.uk/handbook/REC/2.pdf>.

- 1.2.10 LME must continue to fulfil these obligations to maintain its recognition status. Among other things, LME is required to:
- (a) have systems and controls in place to monitor transactions on the LME;
 - (b) retain sufficient financial resources for the performance of its functions as an RIE;
 - (c) operate its markets with due heed to the protection of investors;
 - (d) ensure that trading is conducted in an orderly and fair manner;
 - (e) maintain suitable arrangements for trade reporting;
 - (f) maintain suitable arrangements for the clearing and settlement of contracts;
 - (g) monitor compliance with the LME Rules;
 - (h) enforce the LME Rules;
 - (i) investigate complaints with respect to its business;
 - (j) maintain rules to deal with the default of its Members;
 - (k) co-operate with other regulatory bodies through the sharing of information or otherwise;
 - (l) maintain high standards of integrity and fair dealing; and
 - (m) prevent abuse.
- 1.2.11 On 25 April 1988, the FCA's predecessor organization, the Securities and Investments Board, declared The LME (under its former name, The London Metal Exchange Limited) to be an RIE. The recognition status of RIEs that were recognised by predecessor organizations was grandfathered when the FCA was established in 2013. LME remains compliant with the FSMA Recognition Requirements as demonstrated by its continued status as an RIE. As an RIE, the LME is also a regulated market under the Markets in Financial Instruments (MiFID II) - Directive 2014/65/EU FCA, which has been implemented directly into UK law and applies to RIEs. The FCA is responsible for maintaining the list of regulated markets for which the UK is the Home Member State, which is contained at
- https://register.fca.org.uk/shpo_searchresultspage?preDefined=RM&TOKEN=3wq1nht7eg7tr
- This lists LME as a regulated market. A market may ask to be added to the list of regulated markets if it satisfies the requirements set out in Title III of MiFID. The relevant requirements of Title III of MiFID II have been incorporated directly into the FSMA Recognition Requirements.
- 1.2.12 The FCA has provided guidance on the FSMA Recognition Requirements in its Handbook that sets out the FCA's interpretation of how those obligations might be met in practical terms.
- 1.2.13 The FCA is the authority charged with ensuring that RIEs (such as the LME) continue to comply with the recognition criteria. The FCA has the power to direct any RIE that is failing, or had failed, to comply with the FSMA Recognition Requirements to take action to remedy such non-compliance. It also has the power to censure and /or to revoke the recognition of any RIE that fails to meet the FSMA Recognition Requirements. Accordingly, the LME is subject to the oversight of the FCA.
- 1.2.14 The FCA exercises its supervisory responsibility by conducting an ongoing assessment of whether the LME's rules, procedures and practices are adequate for the protection of investors and for the maintenance of an orderly market in accordance with the FSMA Recognition Requirements (**REC**). For this purpose, the FCA requires LME to report to it, among other things, financial information and changes in its constitution (see REC 3 of the FCA Handbook (<https://www.handbook.fca.org.uk/handbook/REC/3/?view=chapter>)). Further, LME is required to notify the FCA of all rule changes and keeps the FCA notified of significant changes to its rules or procedures before such changes become effective.
- 1.2.15 The formal interaction structure between LME and FCA includes:
- (a) monthly meetings between the FCA and the LME Market Operations department;

- (b) quarterly meetings between the FCA and the LME Head of Compliance;
- (c) quarterly meetings between the FCA and the LME physical operations department;
- (d) half-yearly meetings between the FCA and the LME Business Development department;
- (e) half-yearly meetings between the FCA and the LME Head of IT;
- (f) annual meetings between the FCA and the LME Finance department;
- (g) annual meetings between the FCA and the LME Head of Risk;
- (h) annual meetings between the FCA and the Head of Internal Audit;
- (i) half-yearly meetings between the FCA and the LME Chief Executive Officer;
- (j) half-yearly meetings between the FCA and the Chairman of LME; and
- (k) annual meetings between the FCA and the independent board directors. Informally there are frequent ad hoc contacts between the FCA and the LME. In addition to the LME's formal obligations to notify the FCA, LME consults with the FCA on all material matters.

Rules and policy statements

- 1.2.16 The FCA Handbook is the primary source of rules and policy statements issued by the FCA with respect to the authorisation and continuing oversight of markets, electronic trading systems and clearing organizations. A copy of the full FCA Handbook is available at <https://www.handbook.fca.org.uk/handbook/>. The key rules and policy statements relevant to LME are set out in the FCA's REC Sourcebook.

Financial protections afforded to customer funds

- 1.2.17 The FCA (and other home state regulators in jurisdictions where LME has access) are responsible for regulating the financial soundness and conduct of Members' business.
- 1.2.18 The Client Asset (**CASS**) section of the FCA Handbook sets out the requirements on authorized firms in relation to customer funds. These include requirements such as segregation of customer funds from a firm's own funds and the rules around the distribution of client money in the event that an authorized firm (or third party who holds money on behalf of an authorised firm) fails.

Authorization, licensure or registration of the foreign exchange

- 1.2.19 LME has a statutory obligation to ensure that business conducted by means of its facilities is conducted in an orderly manner and so as to afford proper protection to investors. Failure to comply with this obligation may mean that LME ceases to be an RIE and therefore ceases to be allowed to operate an exchange under FSMA (and therefore also operate as a regulated market under MiFID II).
- 1.2.20 The FCA expects the Audit & Risk Committee of the LME, on behalf of the LME Board, to satisfy itself formally on an annual basis that the LME continues to meet its requirements as a RIE. In order to assist the Audit & Risk Committee in this process, a checklist has been developed, listing all of the FSMA Recognition Requirements and, for each, identifying the systems, procedures and policies in place to demonstrate how each requirement has been met. The Executive Committee reviews and, if content, approves that LME continues to meet the FSMA Recognition Requirements. The Audit & Risk Committee does the same. The FSMA Recognition Requirements for RIEs can be found at: <https://www.handbook.fca.org.uk/handbook/REC/2.pdf>.

1.3 The foreign regulator's approach to the detection and deterrence of abusive trading practices, market manipulation, and other unfair trading practices or disruptions of the market

- 1.3.1 In the UK, the primary term used to describe abusive trading practices, market manipulation and other unfair trading practices or disruptions of the market is "market abuse". In December 2001 the provisions of FSMA relating to market abuse came into force. FSMA prohibited market abuse and gave the FCA the power to issue unlimited fines to penalise market abuse, subject to a right of appeal to the Upper Tribunal.

- 1.3.2 FSMA, as originally enacted, set out three types of market abuse: misuse of non-public material information, the creation of false or misleading market impressions and market distortion. FSMA required the FCA to publish a code describing behaviour which, in its opinion, amounts to market abuse and behaviour which does not (**Code of Market Conduct**). The Code of Market Conduct was implemented on December 1, 2001.
- 1.3.3 In addition to legislation originating from the UK, the LME is subject to EU legislation. The European Market Abuse Regulation (**MAR**) came into effect on 3 July 2016 with the aim of increasing market integrity, investor protection and enhancing the attractiveness of securities markets for capital raising. MAR strengthens the previous UK market abuse framework by extending its scope to new markets, new platforms and new behaviours. It contains prohibitions of insider dealing, unlawful disclosure of inside information and market manipulation, and provisions to prevent and detect these.
- 1.3.4 A key aspect of MAR requires trading venues, such as the LME, to report suspicious transactions and orders (**STORs**). A suspicious transaction or order is one where there are 'reasonable grounds' to suspect it might constitute market abuse.
- 1.3.5 For commodity derivatives, as traded on the LME, the major threat of market abuse is market manipulation. The steps the LME takes to ensure its markets are not easily manipulated are set out in section 5 below. The FCA can also independently enforce the prohibition on market abuse set out in FSMA and the Market Abuse Directive. In order to ensure there is no duplication of effort between LME and the FCA, the FCA has published operating arrangement guidelines which clarify how the LME and the FCA will co-ordinate and co-operate in preventing suspected market abuse.

Laws, rules, regulations and policies that govern the authorization and ongoing supervision and oversight of market intermediaries in the UK

- 1.3.6 The UK has a comprehensive financial services supervision regime. The laws, rules, regulations and policies that govern the authorization and ongoing supervision and oversight of market intermediaries are primarily set out in FSMA and the FCA Handbook.
- 1.3.7 Of the Members that have trading rights, and could therefore deal with customers located in Ontario, the vast majority are companies incorporated in England and Wales. Irrespective of the jurisdiction of incorporation, no Member may undertake any regulated activity in relation to the LME unless it is authorized by the FCA to carry on such regulated activity (see regulation 4.2 of Part 2 of the LME Rules). As a result, all of the trading Members of the LME must comply with FCA rules and are subject to the supervision and oversight of the FCA.
- 1.3.8 The FCA supervises firms according to the risks they present to its statutory objectives. It assesses risks in terms of their impact (the scale of the effect these risks will have on consumers and the market if they were to happen) and probability (the likelihood of the particular issue occurring). The nature and extent of its supervisory relationship with an individual firm depends on how much of a risk it considers that firm could pose to its statutory objectives.
- 1.3.9 Work is co-ordinated through a supervisor with a fixed portfolio of one or more firms that are deemed to carry some risk to the FCA's statutory objectives, who carry out a regular risk assessment (on a cycle of one to four years) and determines a risk mitigation program proportionate to the risks identified. The precise volume and type of work undertaken will depend on the size and riskiness of the firm concerned. Baseline monitoring activities are undertaken for each firm. This involves analysing a firm's financial and other returns, and checking compliance with notification requirements. Breaches and other indicators of risk may be followed up by the supervisory team. For high impact firms, a closer monitoring regime is used (called "close and continuous" work). This is essentially a planned schedule of visits to the firm throughout the regulatory period. This allows the supervisory team to meet the firm's senior management and control functions regularly, and understand and mitigate risk on a real time basis.
- 1.3.10 The FCA and OSC are party to a Memorandum of Understanding Concerning Consultation, Cooperation and the Exchange of Information Related to the Supervision of Cross-Border Regulated Entities (**OSC-FCA MOU**) as shown on the OSC's website: http://www.osc.gov.on.ca/en/About_mou_20130711_nmou-osc-asc-bcsc-uk-fca.htm.

1.4 The protection of customer funds by market intermediaries who may deal with members and other participants located in Canada

- 1.4.1 The UK has a comprehensive regime for the protection of client monies held by investment firms. The FCA's client money rules can be found in CASS Chapter 7 of the FCA Handbook. These rules implement the requirements of MiFID and Article 51 of European Union Directive 2006/73/EC.

Procedures for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk for market intermediaries who may deal with members and other participants located in Canada

- 1.4.2 Cleared Contracts and Client Contracts are “market contracts” under the *Companies Act 1989*. As such, LME Clear and the LME deal with them under their respective default rules in the event of the default of a Member. LME Clear’s Rules and Procedures (the **LME Clear Rules**) apply to Cleared Contracts and the LME Rules apply to Client Contracts.
- 1.4.3 By virtue of section 159 of the *Companies Act 1989*, LME’s default rules, together with those of other recognized investment exchanges and recognized clearing houses (such as LME Clear), take precedence over normal UK insolvency procedures following a default by a Member under an LME contract. This provision is designed to safeguard the operation of the United Kingdom’s financial markets.
- 1.4.4 The default rules of LME are contained in Part 9 of the LME Rules and set out, among other things, the circumstances under which LME may declare a Member to be in default, the actions that LME may take in the event of a default, the type of resources that may be used to satisfy the defaulting Member’s obligations and the sequence in which such resources may be used.
- 1.4.5 Under the Rule 10 of the LME Clear Rules and the LME Clear Default Procedures, LME Clear has a range of options. LME Clear may allow contracts between the defaulting Member and LME Clear to settle or LME Clear can transfer them to another Clearing Member with the consent of the Client and the Member transferee. LME Clear may also conduct an auction of the Defaulting Member’s positions and may ultimately close out the positions themselves.
- 1.4.6 Following the administration of Lehman Brothers, the UK enacted legislation designed to improve UK insolvency law in relation to investment banks, subsequently extended to investment firms. This legislation is known as the Investment Bank Special Administration Regulations 2011 (**SAR**) and came into force in the UK on 8 February 2011. The SAR applies to investment banks which are defined in the *Banking Act 2009* as institutions which: (a) have permission under Part 4 of FSMA to carry on at least one of the following regulated activities: (i) safeguarding and administering investments; (ii) dealing in investments as principal; or (iii) dealing in investments as agent; (b) hold client assets (whether or not on trust); and (c) are incorporated or formed in the UK. SAR sets out specific measures designed to improve the timeliness of the return of client assets. It also requires the special administrator to work with market infrastructure operators (such as the LME and LME Clear).

2 GOVERNANCE

2.1 Governance – The governance structure and governance arrangements of the exchange ensure:

(a) Effective oversight of LME,

- 2.1.1 The governance structure of LME provides for a number of sub-committees, the majority of which report to the board of the LME either directly or through the Executive Committee (**EXCOM**).
- 2.1.2 **EXCOM:** EXCOM is a sub-committee of the board of directors of the LME (the **LME Board**). The LME Board has delegated the running of the day to day operations of the LME to EXCOM.
- 2.1.3 **Operational Committee:** The function of each of the Operational Committees (the metals committees, the Trading Committee, the Traded Options Committee, the Ring Dealers Committee and the Warehousing Committee) is to advise EXCOM in accordance with their terms of reference. These committees contribute to the good governance of the LME, the orderly operation of the market and a close understanding of its participants’ needs. The LME Board has delegated to EXCOM the initial consideration of those recommendations and the power to give effect to a number of those recommendations.
- 2.1.4 **Corporate Governance Committee:** The Audit & Risk Committee and Nomination Committee report directly to the LME Board. The LME User Committee was established to represent the interests and views of the Exchange’s stakeholders and also reports directly to the LME Board. In addition, the Physical Market Committee was established to represent the interests and views of the LME of the physical metals trade and industry and reports to the LME User Committee.
- 2.1.5 **Regulation and Enforcement Committees:** The Arbitration Panel Committee, the Special Committee, the Enforcement Committee and the Quotations Committee are established by the LME Rules. The LME Rules and the terms of reference for these committees set out the functions of these committees and identify those powers that the committees exercise on behalf of the LME Board.

Full details of LME committees and their terms of reference are contained at:

<https://www.lme.com/en-GB/About/Corporate-information/Committees#tabIndex=0>

(b) The LME's business and regulatory decisions are in keeping with its public interest mandate,

- 2.1.6 The Exchange provides the trading environment and regulates the market for the trading of its contracts. Approved as an RIE and a regulated market and conforming with UK and other international regulatory requirements, the LME offers, through price and volume transparency and audit trails, a legally safe forum for metals trading. As an RIE, the Exchange comes under the direct jurisdiction of the FCA.
- 2.1.7 The LME has a statutory requirement to ensure that business on its markets is conducted in an orderly manner, providing proper protection to investors. Regulation of the market is largely carried out by the LME, while the majority of members' business is regulated by the FCA or their home regulator.
- 2.1.8 Beyond this, both the LME and its members are subject to regulatory controls and input from various UK bodies and government offices, as well as EU directives. In international trading, rules applied by overseas regulatory bodies such as the US Commodity Futures Trading Commission (CFTC) also have to be taken into account.

(c) fair, meaningful and diverse representation on the board of directors and any committees of the board of directors, including:

(i) appropriate representation of independent directors, and

- 2.1.9 Best practice in the UK is set by the UK Corporate Governance Code, which requires large UK companies should have at least 50% independent representation on the LME Board. Though the LME is not considered to be a large company the LME complies with best practice and follows this principle. Five of the nine members of the LME Board are independent directors, including the Chairman. There are also extensive requirements relating to the management body of an RIE in the Recognition Requirements, which the LME must demonstrate to the FCA that it meets: see <https://www.handbook.fca.org.uk/handbook/REC/2/4A.html>.
- 2.1.10 Similarly the LME's Audit and Risk Committee and Nomination Committee are comprised of predominantly Independent Directors to ensure sufficient independent judgement on these Committees.

(ii) a proper balance among the interests of the different persons or companies using the services and facilities of the exchange,

- 2.1.11 The LME maintains close links with the market through its Committee structure. Operational Committees have been formed to represent the views of the various sectors that participate in the LME. The Operational Committee advise and make recommendations to the LME's Executive Committee on the working of the Exchange. In addition, the User Committee is a sub-committee of the Board and is charged with representing the users of the LME's direct or indirect services and advising the Board on strategic issues. Further information on the LME's Committee structure can be found on our website (<https://www.lme.com/en-GB/About/Corporate-information/Committees#tabIndex=0>)

(d) The LME has policies and procedures to appropriately identify and manage conflicts of interest, and

- 2.1.12 Under section 175 of the UK Companies Act 2006, a director has a statutory duty to avoid any situation in which he has, or could have, a direct or indirect interest that conflicts, or could conflict, with the interests of the company. Section 175 (2) emphasises the applicability of the duty to the exploitation of any property, information or opportunity and confirms that it is irrelevant whether the company itself could have taken advantage of that property, information and opportunity. There are also provisions regarding the identification and management of conflicts of interest in the Recognition Requirements (see <https://www.handbook.fca.org.uk/handbook/REC/2/5.html>).
- 2.1.13 The LME takes potential conflicts of interest and the associated consequences extremely seriously. It has in place appropriate procedures to mitigate the risk of such occurrences. These procedures supplement the statutory duties on directors set out in the UK *Companies Act 2006*.
- 2.1.14 The articles of association for the LME set out explicit procedures to deal with such scenarios as do the terms of reference for each committee. These procedures are followed as a matter of course.
- 2.1.15 The terms of reference for EXCOM explicitly address the risk of a conflict of interest arising. In addition, the contracts of employment for each of the members of EXCOM address this.

2.1.16 LME Group has also implemented an LME Group Conflicts of Interest Policy which provides employees with an overview of LME's key obligations and the controls implemented in order to identify, manage and disclose actual conflicts of interest.

(e) *There are appropriate qualifications, remuneration, limitation of liability and indemnity provisions for directors, officers and employees of the exchange.*

2.1.17 The Chief Executive Officer of the LME is appointed as a Director. Up to two individuals, who are selected by the Nomination Committee, and approved by the Board, are appointed as independent directors. A further six directors are appointed by the holder of the majority of shares in the LME. Each director is appointed on merit based on skills, qualification and experience. Remuneration is set at Group level and is based on a specific fee structure. Directors' remuneration is solely based on the Boards and Committees they belong to. To avoid a conflict of interest Independent Directors' remuneration is set as a base payment only and does not include performance-related elements. Every Director is entitled to be indemnified by the Company against all costs, charges, losses, expenses and liabilities incurred by him or her in the execution and discharge of his or her duties to the Company or in relation thereto. The Directors' and Officers' Liability Insurance in place provides the Directors with such protection.

2.1.18 Background checks are undertaken against new Directors to ensure that they are fit and proper and eligible to act as a Director. All Directors are also subject to SIF interviews with the FCA, with the regulator providing non-objection to the appointment. The Board is subject to periodic evaluations to ensure that the members, and the Board as a whole, remains fit for purpose and any recommended changes are considered and implemented where appropriate.

2.2 *Fitness – The exchange has policies and procedures under which it will take reasonable steps, and has taken such reasonable steps, to ensure that each director and officer is a fit and proper person.*

2.2.1 Executive Directors are selected from key senior personnel within the HKEX Group and therefore their qualification is through their position. Up to two individuals, who are selected by the Nomination Committee and approved by the Board, are appointed as independent directors. A further six directors are appointed by the holder of the majority of shares in the LME. Each director is appointed on merit based on skills, qualifications and experience. Remuneration is set at Group level and is based on a specific fee structure. Director's remuneration is solely based on the boards and Committees they belong to. To avoid a conflict of interest Independent Directors' remuneration is set as a base payment only and does not include performance-related elements. Every Director is entitled to be indemnified by the Company against all costs, charges, losses, expenses and liabilities incurred by him or her in the execution and discharge of his or her duties to the Company or in relation thereto. The Directors' and Officers' Liability Insurance in place provides the Directors with such protection.

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3 REGULATION OF PRODUCTS

3.1 ***Review and Approval of Products – The products traded on the Exchange and any changes thereto are reviewed by the Foreign Regulator, and are either approved by the Foreign Regulator or are subject to requirements established by the Foreign Regulator that must be met before implementation of a product or changes to a product.***

Product Specifications – The terms and conditions of trading the products are in conformity with the usual commercial customs and practices for the trading of such products.

3.1.1 The FSMA Recognition Requirements and MIFID II establish a range of requirements that must be met before implementation of a product or changes to a product, and on an ongoing basis. In particular, any product admitted to trading on the LME must be capable of being traded in a fair, orderly and efficient manner and must be designed so as to allow for its orderly pricing as well as for the existence of effective settlement conditions. The FCA has adopted guidance in the FCA Handbook which elaborates on the FSMA Recognition Requirements and MIFID II requirements. This guidance sets out principles which the FCA will take into account to determine if the relevant requirements have been satisfied. This guidance are set out at REC 2.12 of the FCA Handbook.

3.1.2 The close and continuous nature of the supervisory interaction with RIEs means that, in practice, the FCA is aware of all proposed new contracts well before they are admitted to trading, and if there is a regulatory concern, then this will be built into the formulation of the contract specifications at that time. LME must confirm in writing to the FCA that any new contract complies with the relevant requirements and provides a regulatory analysis to evidence how such

compliance will be achieved. The FCA will then perform an internal review and, subject to any questions or concerns it may wish to discuss with the LME, it provide its non-objection ahead of launch.

3.2 ***Risks Associated with Trading Products – The Exchange maintains adequate provisions to measure, manage and mitigate the risks associated with trading products on the exchange, including, but not limited to, margin requirements, intra-day margin calls, daily trading limits, price limits, position limits, and internal controls.***

3.2.1 Trades on the LME are cleared through LME Clear (see paragraph 29 of Part I). Each Member provides LME Clear with, and maintains on a daily basis for so long as it is a Member, eligible collateral with a Collateral Value sufficient to satisfy its Margin Requirement, which comprises of:

- (a) the End of Day Margin Requirement;
- (b) the Intra-Day Margin Requirement(s); and
- (c) any other margin requirements (which excludes a Default Fund Contribution) required at any time by LME Clear pursuant to the Rules and the Procedures,

as security, cover and/or credit support for the performance by that Member of all of its present and future obligations to LME Clear pursuant to the Rules or the operation of the Clearing System.

4 ACCESS

4.1 Fair Access

(a) ***The exchange has established appropriate written standards for access to its services including requirements to ensure:***

- (i) ***Participants are appropriately registered as applicable under Ontario securities laws or Ontario commodity futures laws, or exempted from these requirements,***
- (ii) ***The competence, integrity and authority of systems users, and***
- (iii) ***Systems users are adequately supervised.***

(b) ***The access standards and the process for obtaining, limiting and denying access are fair, transparent and applied reasonably.***

(c) ***The exchange shall not unreasonably prohibit, condition or limit access by a person or company to services offered by it.***

(d) ***The exchange does not***

- (i) ***permit unreasonable discrimination among participants, or***
- (ii) ***impose any burden on competition that is not reasonably necessary and appropriate.***

Access requirements

4.1.1 As a UK Recognised Investment Exchange, the LME is subject to UK regulatory requirements that are closely aligned with those outlined above. The LME is obligated under the Financial Services and Markets Act 2000 (Recognition Requirements) Regulation 2001 (SI2001/995) (the **Recognition Regulations**) and (b) the FCA rules applicable to recognised investment exchanges (the **REC handbook**), to ensure that access to its facilities is fair and non-discriminatory. In particular, the LME is required to “make transparent and non-discriminatory rules, based on objective criteria, governing access to, or membership of, its facilities” (REC 2.7.1A). Any new LME initiative is assessed in detail against the Recognition Regulations and such assessment provided to the FCA so the FCA can provide non-objection.

4.1.2 LME's admittance criteria are publicly available and are applied equally to all applicants. Access requirements for prospective LME participants are set out in Part 2 of the LME Rules. Part 2 specifies the requirements that are applicable to each category of Member, including for instance the prospective Member's legal structure, regulatory status, capital holdings, AML and financial crime procedures, This is supplemented by a jurisdictions document published on the LME website which specifies additional requirements or constraints that are applicable to Members

located in specific jurisdictions in order to ensure compliance with applicable law (see paragraph 4.1.8 below for further detail in relation to this document).

- 4.1.3 The LME has in place a process for appealing decisions to deny or limit access to its services (see Regulations 5.7 to 5.9 of the LME Rules). Necessary electronic and physical records in relation to any such appeals are held in confidence and for the appropriate period of time in accordance with our record retention policy, in accordance with our legal, compliance and regulatory requirements.
- 4.1.4 No Member may undertake any regulated activity in relation to the LME unless it is authorized (including by exemption – e.g. in relation to Members based outside of the UK, in other countries, states and provinces and territories, who have been authorized by their home regulator) by the FCA to carry on such regulated activity (see regulation 4.2 of Part 2 of the LME Rules). As a result, all trading (Category 1, 2, 3 and 4) Members must comply with the FCA rules. Members must inform LME immediately of any variation, cancellation or permission to carry on a regulated activity (regulation 4.3 of Part 2 of the LME Rules).
- 4.1.5 The ability to handle customer business through the issue of Client Contracts means that Category 1, 2 and 4 Members must at all times be regulated for this specific purpose by the FCA or an equivalent regulator. When an applicant applies for membership of LME, the applicant must confirm its regulatory status and FCA registration number (where applicable), and this is validated by LME. A similar process will be implemented for Members based in Ontario.
- 4.1.6 No person may apply or continue to be a Category 1, 2, 3 or 4 Member unless such person is:
- (a) an authorized person or exempt person within the meaning of Part III of the FSMA; or
 - (b) an investment firm authorized under Article 5 of MiFID by the competent authority of an European Economic Area (**EEA**) state other than the UK (include a branch established in the UK of such a firm); or
 - (c) a credit institution authorized under the Banking Consolidation Directive by the competent authority of an EEA State other than the UK (including a branch established in the UK of such an institution); or
 - (d) a person whose activities in relation to the Exchange as a Member would not constitute regulated activities (as defined in FSMA) on the basis of an appropriate exclusion under the RAO.
- 4.1.7 No Member may undertake any regulated activity (as defined in the FSMA) in relation to the Exchange unless the Member is:
- (a) authorized, including through exemption, by the FCA to carry on such a regulated activity; or
 - (b) a person whose activities in relation to the Exchange as a Member would not constitute regulated activities (as defined in FSMA) on the basis of an appropriate exclusion under the RAO.
- 4.1.8 The LME Rules do not allow a person to enter into a Client Contract unless he or the other party to the Contract is a Category 1, 2 or 4 Member that can validly enter into Client Contracts in accordance with the law of the UK and any other applicable law or regulation.
- 4.1.9 In relation to ensuring that participants are appropriately registered as applicable under Ontario securities laws or Ontario commodity futures laws, or exempted from these requirements: the LME is regulated by a number of overseas regulators in a manner similar to that sought in Ontario (including in the US by the CFTC, in Australia by ASIC, in Singapore by MAS, and in Hong Kong by the SFC, amongst others). It is therefore familiar with local regulators imposing particular requirements as a result of local law and regulation. The LME ensures that its participants comply with these requirements through its jurisdictions document, which is can be found on the website at <https://www.lme.com/About/Regulation>. Members are obliged to comply with the jurisdictions document by virtue of Regulation 12.6(h) of Part 2 of the LME Rules, which states that “A Member shall observe the requirements relating to participants from jurisdictions other than the UK, as set out in the document headed "Jurisdictions" which shall be available on the website of the Exchange, as such document is updated from time to time”.
- 4.1.10 Once it obtains exemption in Ontario, the LME will incorporate the specific requirements relating to Ontario into the jurisdictions document, in particular those relating to participants on its market which are set out in the proposed terms and conditions to the draft exemption order.

Due diligence and on-going supervision

- 4.1.11 The LME conducts a robust due diligence procedure to ensure that its Members are fit and proper, in order to protect the integrity of the LME and the orderliness of its market. In relation to systems access, pre-admittance requirements are in place in relation to systems training, conformance, testing and accreditation. Once a Member has been admitted, controls are also applied to any additional system users. System users are also subject to supervision on an on-going basis, in particular in the form of oversight by the Trading Operations and Post-Trading Operations and Market Surveillance teams).
- 4.1.12 Annual due diligence is performed as a mechanism for monitoring qualifying members' continued suitability. This takes the form of a risk-based approach using a Member risk assessment model. This is updated annually and targeted assessments are performed according to the determined risk ratings. A real-time due diligence screening tool is also used to ensure continued suitability. Member audits are also conducted to ensure that all Members have appropriate systems and controls to ensure ongoing compliance with the LME Rules and Notices. Such reviews may be either desk based or on-site visits.

5 REGULATION OF PARTICIPANTS ON THE EXCHANGE

Regulation – The Exchange has the authority, resources, capabilities, systems and processes to allow it to perform its regulation functions, whether directly or indirectly through a regulation services provider, including setting requirements governing the conduct of its participants, monitoring their conduct, and appropriately disciplining them for violations of exchange requirements.

5.1 Members and other participants are required to demonstrate their compliance with these requirements

- 5.1.1 The LME Rules state Contracts may be written only by Category 1, 2 and 4 Members and accordingly at least one party to every Contract must be such a Member; non-Members of the LME cannot have direct access to LMEselect. Whatever the form of the electronic connection, orders placed by non-Members will always be routed through a Member and the counterparty risk to non-Members will always be carried by an LME Category 1, 2 or 4 Member.
- 5.1.2 All Members are required by LME to satisfy the membership criteria on an ongoing basis. Members are required to notify the LME of anything the LME might reasonably expect to be disclosed to it (see regulation 9.6(d) of Part 2 of the LME Rules). This would include all legal, financial and regulatory matters that are material to their standing as Members.
- 5.1.3 Under the LME Rules, trades on LMEselect will always be routed through an LME Category 1, 2 or 4 Member. As such, other than Members, there are no other participants to which separate requirements for participation on LMEselect may apply.
- 5.1.4 Regulation of the market is carried out by the LME, while the FCA is responsible for regulating the financial soundness and conduct of Members' business (unless the Member is not FCA authorized such as an unauthorised overseas person (UOP). The FCA (or other regulatory bodies if the Member benefits from the UOP exemption) and LME monitor Members on an ongoing basis to confirm that Members are in full satisfaction of their respective regulatory obligations. UOPs are required to provide a legal opinion for the benefit of the LME confirming that they will benefit from the exemption and this opinion will be refreshed periodically, including in response to a material change in the LME Rules.
- 5.1.5 The FCA rules require relevant personnel of FCA authorized firms to have applicable demonstrable experience in relation to the regulated activities which the firm is permitted to perform. The FCA monitors these authorized firms and the quality of the personnel in key operations and compliance functions. For more information on the rights and obligations of Members towards the FCA, please refer to the above sections 4.1.4 to 4.1.7.
- 5.1.6 The financial resource requirements, standards, guides or thresholds required of Members are set out at Part 2 of the LME Rules. Regulation 9.1.1 of Part 2 of the LME Rules requires each Member to submit annual audited accounts within four months of the end of the financial year as well as for those of its ultimate parent undertaking. This information is used to verify that Members have complied with the financial resource requirements set out in the LME Rules.
- 5.1.7 LME Clear (which has counterparty risk exposure to Category 1, 2 and 3 Members through the clearing of Cleared Contracts) constantly monitors the collateral requirements for Members. The FCA (whose rules each Category 1, 2, 3 and 4 Members must comply with, unless the Member is a UOP) monitors the financial soundness of Members on an ongoing basis. The FCA is responsible for regulating the financial soundness and conduct of Members' business, unless the Member is a UOP. The admission process for becoming an FCA regulated firm includes a fit and proper person test.

5.2 Client Advisory and Member Services

- 5.2.1 The LME Market Access Department (**Market Access**) is responsible for the on-boarding of new entities into the LME Base Service, LMEprecious, LMEshield and LMEbullion (the **Services**). A description of each of those Services is set out in paragraphs 5.2.3-5.2.7 below. The Market Access function is, in addition, responsible for confirming the on-going suitability of members within the Services. Applicants for LME membership are required to meet the relevant eligibility criteria as set out in Part 2 of the LME Rulebook (Membership, Enforcement and Discipline).
- 5.2.2 Members must provide the information necessary to confirm their continued compliance with the eligibility criteria set out in the LME Rulebook. Market Access conduct a risk based approach in respect of reviews demonstrating that the LME discharges its obligations with respect to the UK Money Laundering Regulations and the LME's Financial Crime Policy.
- 5.2.3 The LME Base Service refers to the availability of the facilities of the London Metal Exchange for the trading of contracts relating to non-precious metals.
- 5.2.4 LMEprecious refers to the availability of the facilities of the LME for the trading of LMEprecious Futures. An LMEprecious future is a cleared, physically settling exchange-traded futures contract which has any Precious Metal as its underlying (namely, Gold or Silver).
- 5.2.5 LMEshield refers to the LME's central electronic register that provides global off-warrant commodity receipting. LMEshield immobilises paper receipts and uses electronic versions in the system. This facilitates lending by addressing uncertainties surrounding commodity receipts as collateral and reducing the risk of fraud on financed material.
- 5.2.6 LMEbullion refers to the LME's custom-built electronic auction system for platinum and palladium, which was launched in December 2014. It was designed in close consultation with the precious metals community to combine the best elements of an electronic platform with Platinum Group Metals (PGM) fixing methodologies. LMEbullion delivers fully automated price display auctions enabling twice-daily price discovery and price dissemination via licenced data distributors.

5.3 Enforcement of LME Rules on Members

- 5.3.1 The LME Market Surveillance function consists of approximately ten staff. The Enforcement function is undertaken by members of the LME Legal team.
- 5.3.2 The primary role of the LME Market Surveillance team is to protect the integrity of the LME's markets by monitoring activity across all LME trading venues for behaviour which could be indicative of possible market abuse under the Market Abuse Regulation (**MAR**). The MAR contains prohibitions on insider dealing, unlawful disclosure of inside information and market manipulation. LME Market Surveillance utilises a bespoke electronic surveillance system (referred to as the **EDW** surveillance system) which is alert based, allowing the team to monitor for behaviour that may be abusive, manipulative or undermine the integrity of the Exchange. This monitoring covers market orders and trades through all LME trading venues (LMEselect, the Ring and the Interoffice market) on a T+1 (trade date plus one business day) basis. The Market Surveillance team also utilises a case management tool to document all alerts generated by the electronic surveillance system and provide a full audit trail of all analysis and communications. In addition, the Compliance Monitoring System (**CMS**) market replay function allows the team to play back historical order book activity to review market conditions at a given point in time. The system gives a comprehensive view of the order book.
- 5.3.3 The LME Market Surveillance team is also responsible for enforcing the LME Lending Rules. Category 1, 2, 3 and 4 Members are required to report, on a daily basis by way of the LME's Daily Position Reporting System, all holdings and positions for both house and client accounts. The LME Market Surveillance team examines data relating to Members' and their clients' futures, options and warrant positions, as electronically reported by Members each day. The information is analysed in conjunction with data on underlying trends in supply and demand and on traded prices in order to detect any potential tightness, squeezes or anomalies in the market. For this purpose, LME Market Surveillance uses a system referred to as Client Support System (**CSS**). CSS is used by the LME Market Surveillance team to monitor the positions of Members and their clients and to assist with the administration of the Lending Rules. It provides the LME Market Surveillance function with the key information it needs to ensure the LME maintains an orderly market. The information in CSS is used to verify information submitted by Members via the Daily Position Reporting System. CSS is a local client application which receives detailed position reporting files before 8.30am London time each morning, reflecting positions as of the close of business the previous day. It therefore provides an overview of positions of Members and clients down to one lot.

- 5.3.4 The Lending Rules require that Members holding positions above a certain level be prepared to lend to the market, thereby providing liquidity. This prevents dominant holders from squeezing the market, taking advantage of price movements caused by that dominant position and damaging market integrity.
- 5.3.5 The LME Market Surveillance team also receives and investigates referrals of unusual activity from other areas of the LME. For example, the LME Market Surveillance team works closely with the LMEsmart and LMEselect teams. The 'LMEselect team' in this context refers to Trading Operations. Trading Operations establish the LME's reference prices and have responsibility for monitoring the market in real-time on LMEselect. This includes, for instance, enforcement of the LME's policies in relation to error trades and erroneous submissions. Trading Operations may identify activity or behaviour which may warrant further investigation and this is escalated to the Market Surveillance team as appropriate. The 'LMEsmart team' in this context refers to Post Trade Operations, who are the Business Owners of the LME's matching service (LMEsmart). LMEsmart provides a post-trade registration and matching service for all LME trading venues. The Post Trade Operations team also own the LME's matching rules and has additional governance over further LME systems such as LMEsword (the LME's secure electronic transfer system for LME warrants) and LMEshield (which is the LME's central electronic register providing global off-warrant commodity receipting). Post Trade Operations work closely with Market Surveillance regarding the member audit process to ensure that Members are registering transactions within the spirit of the LME matching rules. Post Trade Operations will also escalate concerns that have been observed when interacting with the membership that might require further investigation by Market Surveillance. LME Market Surveillance also monitors stock movements and trade matching performance.
- 5.3.6 As stated above, the EDW surveillance system monitors trading and order book data on a T+1 (trade date plus one business day) basis and is used by Market Surveillance to detect market patterns or trading strategies which may be deemed abusive or manipulative and may require further investigation. The system is designed to meet the standards required under the European Securities and Markets Authority (**ESMA**) Guidelines on systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities.
- 5.3.7 The EDW surveillance system processes all order and trade data across of trading platforms operated by the LME. Specifically, there are six separate EDW alert engines which use alerting algorithms to interrogate the data and generate electronic surveillance alerts across 18 different alert scenarios. These scenarios include but are not limited to insider trading and different types of possible manipulation. The team also utilises the CMS Market Replay tool which enables the user to recreate the electronic order book at any given point in time.
- 5.3.8 Following analysis by LME Market Surveillance, suspicions of possible market abuse are escalated to the LME Referrals Committee for discussion to determine whether the activity should be submitted to the UK FCA as a Suspicious Transaction and Order Report (**STOR**). If considered appropriate, LME Market Surveillance can also instigate a formal investigation into the activity of a Member which may result in possible enforcement action and sanction.
- 5.3.9 Furthermore, all trade data is stored in a web based database tool called Trade Analytics. This includes enriched data such as reference fields and customer account fields. Where required, the data can be presented at trade-half level, i.e. each buy and sell side contains unique data. With this structure Trade Analytics is able to present data at a granular level, illustrating information such as position movements of an individual client across several brokers. This level of granularity is necessary to be able to reconstruct trade flow and assist surveillance and investigation.
- 5.3.10 The Market Surveillance team also assesses Member compliance with the LME Rules and associated Notices. This is achieved through a risk based Member Audit Programme via a series of thematic desk-based reviews. An annual Member audit plan is agreed with senior management to ensure that there is appropriate coverage of the LME Member base and that all required Rules and Notices are included in the review programme. In determining the plan, team members take into account issues raised by other areas of LME Market Surveillance and the wider Market Operations department so that a holistic approach can be taken. At the commencement of an audit, Members are required to provide information or data so that a desk based review can be conducted. LME Market Surveillance also has the power to conduct a site visit if required. If considered appropriate, LME Market Surveillance can also instigate a formal investigation into a Member should the audit determine that the Member's systems and controls are not adequate. The Member Audit Programme therefore contributes to ensuring that Members uphold the expected standards and that the integrity of the market is maintained.
- 5.3.11 The LME Member Audit programme also covers systems access which ensures that Members only grant LMEselect access to relevant personnel and maintain the necessary records in accordance with LME requirements. Breaches of LME Rules may result in formal investigation and possible enforcement action.
- 5.3.12 Possible breaches of LME Rules may be subject to formal investigation by the LME Market Surveillance and Legal teams. In the event that a breach of LME Rules has taken place, the matter may be further investigated for possible consideration by the LME Enforcement Committee. The LME Enforcement Committee will consider the case presented

and in the event that it determines that enforcement action is appropriate, determine what sanction should be imposed on the Member. The LME has brought a number of successful enforcement actions against members in recent years, see for example:

<https://www.lme.com/en-GB/Search?keywords=citigroup>

<https://www.lme.com/en-GB/Search?keywords=disciplinary%20action>

- 5.3.13 The LME compliance and surveillance functions are divided as a matter of policy by means of information barriers from the rest of the LME so as to preserve the confidentiality of sensitive Member and client commercial information that is required for regulatory purposes.
- 5.3.14 The LME has certain summary powers to deal with market emergencies that apply in addition to the Lending Rules. In the event of a suspected undesirable or improper trading practice such as an attempt to squeeze the market, the LME's Special Committee may take any steps necessary to resolve the situation. These steps include ordering a Member to trade out of positions. The Special Committee is comprised of independent non-conflicted persons appointed by the LME Board. This ensures that no directors who may have a conflict of interest are involved in decisions made about any market aberrations. The powers of the Special Committee to intervene in the market in emergencies are set out in Regulation 17 of Part 3 of the LME Rules (<https://www.lme.com/About/Regulation/Rules/Rulebook>).

LME's capacity to detect, investigate, and sanction persons who violate LME Rules

- 5.3.15 Regulations 9 to 12 of Part 2 of the LME Rules set out the capacity of LME to investigate and sanction persons who violate LME Rules. This function, along with the detection of such violations, is performed by LME Market Surveillance functions as set out above.
- 5.3.16 Regulations 9.6 and 9.7 of Part 2 of the LME Rules prohibit fraud and abuse (including, but not limited to, wash sales and trading ahead) as well as other trading practices and market abuses. UK and European legislation supplement these prohibitions.
- 5.3.17 LME Market Surveillance has sufficient personnel, and sufficient software tools, to monitor the trading venues operated by the LME. The Trading Operations team also monitors the real time market, including the enforcement of orderly trading in the Ring (open outcry). The LMEselect Trading Operations team also monitors for orderly trading on LMEselect and enforces the LME's order to trade ratio and message throttling policies. Analysis of trading in the Ring, on LMEselect and in the Inter-office market (telephone) for potential market abuse is conducted by LME Market Surveillance. Trading Operations establish the LME's reference prices and monitor the market in real-time on LMEselect. Part of this monitoring includes enforcement of the LME's policies in respect of error trades and erroneous submissions, and its dynamic price banding. As a result of daily monitoring of the real-time market, Trading Operations may identify activity or behaviour which warrants further investigation or analysis (examples include but are not limited to: unusual price movements in the real-time market, or order behaviour which may be detrimental to the integrity of the market). Such activities or behaviours are escalated to Market Surveillance as appropriate. Market Surveillance receives referrals of such activity from Trading Operations for further analysis and information gathering (including requesting further information directly from the Member). Such referrals and the results of analysis are also escalated to the weekly LME Referrals Committee (which consists of senior staff from Market Operations and Legal) to determine whether the behaviour should be the subject of a formal investigation and / or referred to the appropriate regulatory body. The resourcing of the LME Legal and Regulation, Risk and Compliance team is kept under constant review. Oversight of the Market Surveillance teams is undertaken by the Head of Market Surveillance, who reports directly to the Chief Operating Officer. The surveillance team is comprised of approximately twelve staff. Internal compliance and regulatory policy is undertaken by the Regulation, Risk and Compliance department, which has approximately ten staff in total.
- 5.3.18 Regulation 9 of Part 2 of the LME Rules sets out comprehensive obligations on Members to provide the LME access to information, including in relation to Over-The-Counter transactions and information held by third parties. Regulation 10.5 of Part 2 of the LME Rules supplements this obligation, but this regulation will only apply where there is an investigation.
- 5.3.19 Members must submit to the regulation of the LME as a condition of access to the LME market. Regulation 2.4 of Part 1 of the LME Rules stipulates that the LME Rules shall be binding on all members. Regulation 1.4 of Part 3 of the LME Rules specifies that all Client Contracts may only be written by Category 1, Category 2 or Category 4 Members, the effect of which is that all client contracts will have at least one party being a Member. Regulation 1.5 of Part 3 of the LME Rules specifies that all client contracts shall be governed by the LME Rules.

6 RULEMAKING**Purpose of Rules**

- (a) *The exchange has rules, policies and other similar instruments (“Rules”) that are designed to appropriately govern the operations and activities of participants.*
- (b) *The Rules are not contrary to the public interest and are designed to*
- (i) *ensure compliance with applicable legislation,*
 - (ii) *prevent fraudulent and manipulative acts and practices,*
 - (iii) *promote just and equitable principles of trade,*
 - (iv) *foster co-operation and co-ordination with persons or companies engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in products traded on the exchange,*
 - (v) *provide a framework for disciplinary and enforcement actions, and*
 - (vi) *ensure a fair and orderly market.*

6.1 The LME Rules are available on the LME website (<https://www.lme.com/About/Regulation/Rules/Rulebook>) (the **LME Rules**). The LME Rules are separated into 13 parts and each part focuses on a specific area. In addition, the LME has the power to issue Notices, which, pursuant to Regulation 2.2 of Part 1 of the LME Rules, have the force of rules. The key notices which are related to Member compliance are set out on the LME website at

<https://www.lme.com/About/Regulation/Rules/Notices>.

6.2 The LME Rulebook and Notices are binding on all Members. In order to become a member, applicants must sign a membership agreement with the LME undertaking to be bound by the LME Rules.

6.3 As a RIE under FSMA, the LME is obliged to adhere to the FSMA Recognition Requirements. The FSMA Recognition Requirements specify that the LME must ensure that appropriate procedures are adopted for it to make rules, for keeping its rules under review and for amending them. The FCA has adopted guidance in the FCA Handbook which elaborates on the Recognition Requirements. This guidance sets out principles which the FCA will take into account to determine if the above requirement has been satisfied. This guidance is set out at REC 2.14 of the FCA Handbook (see <https://www.handbook.fca.org.uk/handbook/REC/2/>).

6.4 Pursuant to section 293(5) of FSMA, whilst there is no formal approval requirement for rules, if the LME alters or revokes any of its rules or guidance, or makes new rules or issues new guidance it must give written notice to the FCA. Further, the combination of a legal requirement to consult on rule changes, and the ‘close and continuous’ nature of the supervisory interaction with RIEs means that, in practice, the FCA is aware of all material proposed rule changes well before they are made, and if there is a regulatory concern, then this will be built into the formulation of those rules. For example as part of the monthly meetings between the FCA and the LME Market Operations department, the LME notifies the FCA of any forthcoming changes to the LME Rules that relate to trading rules of the LME. The FCA also receives copies of all Notices issued by the LME. Should the FCA wish to review proposed changes to the LME Rules, it will request further information from the LME, which the LME will provide. In such instances, the FCA and the LME will work closely to produce a form of wording that is acceptable to both entities. In addition, section 300A of FSMA (introduced by the Investment Exchanges and Clearing House Act 2006) gives further powers to the FCA in respect of rules which may amount to an “excessive regulatory provision”, requiring a formal notification process and right for the FCA to disallow any such rules. Finally, for any major changes to the LME Rules (such as new contracts, structural and other changes) and other significant initiatives, the LME will prepare a detailed regulatory analysis, referred to as a “REC analysis”, which details how the LME will comply with all relevant provisions of REC following the change.

6.5 The LME Rules have been designed to ensure compliance with all applicable legislation and to ensure a fair and orderly market. The LME has an internal Compliance department which, amongst other things, monitors the LME’s compliance with all applicable legislation. The Compliance Monitoring Programme (**CMP**), which is maintained by Compliance, lists all legislation applicable to the Exchange on a line-by-line basis and explains how the LME complies with such legislation.

6.6 The LME Rules have extensive provisions regarding the conduct of Members. These include provisions relating to “prohibited practices” (see Regulation 14 of Part 3 of the LME Rules), which are designed to prevent fraudulent and manipulative acts and practices. More generally, the provisions of Part 3 (Trading Regulations) and Part 4 (Contract Regulations) are designed to set out how trading on the LME should take place in a fair and orderly manner and have been designed to ensure just and equitable principles of trade and to foster co-operation and co-ordination with persons or companies engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in products traded on the Exchange.

6.7 Part 2 of the LME Rulebook sets out the requirements for admission to membership, as well as provisions relating to provision of information and discipline / enforcement. Regulation 12 of Part 2 of the LME Rules sets out the obligations of Members to promptly provide information reasonably requested by the exchange. Part 2 also sets out the ability of the LME to investigate and take disciplinary action against members for suspected breaches of the Rules. The provisions relating to investigations are set out at Regulation 13 of Part 2, and the provisions relating to discipline are set out at Regulation 14 of Part 2. Pursuant to Regulation 14.22, a Disciplinary Committee has broad powers to impose penalties on members, including a reprimand, a fine, an order that the Member make restitution to any person when the Member has profited from an act of misconduct at that person's expense, a requirement to comply with such terms and conditions as appropriate, and suspension or expulsion from membership.

Enforcement of the LME Rules

6.8 The LME has extensive compliance and surveillance functions which ensure that LME Rules are being followed. The surveillance function is split between two divisions; the Market Surveillance team, and Market Access (see paragraphs 5.2.1-5.2.2 above). The surveillance functions consist of approximately ten staff, whilst the Market Access division consists of approximately three staff. The LME also has an enforcement team made up of members of the Legal team.

6.9 The primary role of the LME Market Surveillance team is to protect the integrity of the LME's markets by monitoring that trading is fair and transparent. The LME Market Surveillance staff analyse confidential data relating to members' and their clients' futures, options and warrant positions, as electronically reported by members each day. The information is analysed in conjunction with data on underlying trends in supply and demand and on traded prices in order to detect any potential tightness, squeezes or anomalies in the market. Any concerns about suspected abuses of the market will be discussed with the member(s) concerned and, if necessary, referred to the enforcement team for further review and scrutiny (see paragraph 5.3 above).

6.10 The LME Market Surveillance team also ensures that the market remains orderly. As part of this, it is responsible for the application of Position Management through administering the Lending Rules, Position Monitoring and Accountability Levels. It also monitors the registration and matching of trades to ensure this takes place within the time frames prescribed by the LME. Furthermore, it monitors intra-day trading activities through EDW, alongside the LMEselect and LMEsmart system teams, in close liaison with LME Clear. In so far as LMEselect is concerned, the LME Market Surveillance team oversees that all trading on LMEselect takes place in accordance with the LME Rules.

6.11 The Market Surveillance team also utilizes the bespoke trade surveillance system, EDW. The system is alert and report based, allowing the surveillance team to monitor for behaviour that may be abusive, manipulative or undermine the integrity of the exchange. The monitoring covers market orders and trades through LMEselect, the Ring, the inter-office market and trades entered into LMEsmart on a T+1 (trade date plus one business day) basis. The Market Surveillance team utilizes Jira as the case management tool to investigate and document all alerts generated by the EDW alert engine. In addition the Compliance Monitoring System (CMS) market replay function allows the team to playback historical market activity to review market conditions at a given point in time. The system gives a comprehensive view of the market and enables the LME to react to changes in market conditions.

6.12 The Market Surveillance team also assesses Member compliance with the LME Rules and associated notices. This is done through the Member Audit Programme (MAP) via a series of desk-based reviews. This programme allows the Market Surveillance team to focus on any particular rule or theme it feels may be pertinent in conjunction with EDW, the LME Market Surveillance team and its wider view of the market. In so doing, the MAP allows the Market Surveillance team to have a holistic approach in ensuring members are upholding the standards expected from the exchange and maintaining the integrity of the market.

6.13 Market Access (formerly Client Advisory and Membership Services): Market Access works closely with the LME Market Surveillance team to review members' controls, procedures and general compliance with the LME Rules on application for membership of the LME. In addition, the LME compliance and surveillance functions together review the controls and procedures put in place by LMEselect participants to ensure that only accredited users access LMEselect and LMEselect participants maintain the necessary records in accordance with LME and FCA requirements. Breaches of LME Rules will be referred to the enforcement team for further scrutiny.

Rule Changes

- 6.14 The FSMA Recognition Requirements specify that the LME must ensure that appropriate procedures are adopted for it to make rules, for keeping its rules under review and for amending them. The FCA has adopted guidance in the FCA Handbook which elaborates on the FSMA Recognition Requirements. This guidance sets out principles which the FCA will take into account to determine if the above requirement has been satisfied. This guidance is set out at REC 2.14 of the FCA Handbook.
- 6.15 Pursuant to section 293(5) of the FSMA, while there is no formal approval requirement for rules, if LME alters or revokes any of its rules or guidance, or makes new rules or issues new guidance it must give written notice to the FCA. Further, the combination of a legal requirement to consult on rule changes, and the close and continuous nature of the supervisory interaction with RIEs means that, in practice, the FCA is aware of all material proposed rule changes well before they are made, and if there is a regulatory concern, then this will be built into the formulation of those rules. For example as part of the monthly meetings between the FCA and the LME Market Operations department, LME notifies the FCA of any forthcoming changes to the LME Rules that relate to trading rules of LME. The FCA receives copies of all notices issued by LME. Should the FCA wish to review proposed changes to the LME Rules, it will request further information from the LME, which LME will provide. In such instances, the FCA and LME will work closely to produce a form of wording that is acceptable to both entities. In addition, section 300A of FSMA (introduced by the Investment Exchanges and Clearing House Act 2006) gives further powers to the FCA in respect of rules which may amount to an “excessive regulatory provision”, requiring a formal notification process and right for the FCA to disallow any such rules. Therefore, as noted above, for any major changes to the LME Rules (such as new contracts, structural and other changes) and other significant initiatives, the LME will prepare a detailed regulatory analysis, referred to as a ‘REC analysis’, which details how the LME will comply with all relevant provisions of REC following the change.

7 DUE PROCESS

Due Process – For any decision made by the exchange that affects a participant, or an applicant to be a participant, including a decision in relation to access, exemptions, or discipline, the exchange ensures that:

- (a) parties are given an opportunity to be heard or make representations, and***
- (b) it keeps a record of, gives reasons for, and provides for appeals or reviews of its decisions.***

- 7.1 The Market Surveillance and enforcement teams (as referenced above in section 5 above) are governed by the following procedures:
- 7.2 Regulations 13 and 14 of Part 2 of the LME Rules respectively set out the investigatory and disciplinary procedures of the LME. The LME has wide powers to investigate suspected acts of misconduct by members. Any suspected act of misconduct will be investigated by the Market Operations and Legal functions. A report detailing the findings of the investigation shall be passed to the Head of Market Operations who may, or may not, recommend to the Enforcement Committee that disciplinary proceedings should be commenced. Where the Enforcement Committee decides to institute disciplinary proceedings, a Notice, approved by it setting out the alleged act of misconduct together with a summary of the facts relied upon (“the **Notice**”) shall be served on the Member concerned. The Member has twenty working days from service of the Notice in which to serve a statement of defence (the **Defence**) responding to all or any of the allegations, stating its intended pleas and what admissions of fact, if any, it makes. Generally in practice the LME and the Member will settle the enforcement action (pursuant to Regulations 14.36 to 14.41) prior to the service of the Defence. However, if the matter is not settled, the matter may proceed to a Disciplinary Committee.
- 7.3 A Disciplinary Committee drawn from the Disciplinary Panel will determine the outcome of the proceedings (Regulations 14.16 to 14.21 of Part 2 of the LME Rules). Regulations 14.22 to 14.26 of Part 2 empower a Disciplinary Committee to impose penalties on a member, including to fine, suspend or expel any Member pursuant to fair and clear standards.
- 7.4 A Member may appeal the decision of the Disciplinary Committee to an Appeal Committee drawn from the Appeal Panel (Regulations 14.27 to 14.35 of Part 2 of the LME Rules).
- 7.5 The membership and composition of a Disciplinary Committee and Appeal Committee is set out by Regulations 14.47 to 14.60 of Part 2 of the LME Rules. The Disciplinary Panel and the Appeal Panel are staffed by independent and impartial experts, who are generally former senior members of the judiciary of the English courts or experienced former senior regulators or business people. The members of the Disciplinary Panel and Appeal Panel are set out on the LME website: <https://www.lme.com/en-GB/About/Corporate-information/Committees#tabIndex=0>

- 7.6 There is no explicit power for the LME to issue warning letters to Members. Despite this, the LME does issue such letters in relation to infractions of the LME Rules such as a failure to comply with Regulation Rule 12.6 of Part 2 of the LME Rules (organising and control of a Member's internal affairs). These letters are usually issued with a view to evidencing at a later date a systematic failure to maintain such controls through repeated breaches. The FCA is kept fully abreast of all instances in which such warnings are issued.
- 7.7 Pursuant to English administrative law, the outcome of a Disciplinary Appeal Committee may be subject to judicial review by the English Courts.
- 7.8 The Head of Market Operations may publish the findings of an investigation where some or all of the findings may be of relevance to the market (Regulation 10.7 of part 2 of the LME Rules). The outcome of disciplinary proceedings may be notified to the relevant parties (Regulation 11.42 to 11.45 of Part 2 of the LME Rules). The definition of the relevant parties depends on the facts of each disciplinary proceeding. However, since 1998, the LME has made public the outcome of all disciplinary proceedings.
- 7.9 Provisions relating to applications for membership are set out in the LME Rulebook at Regulation 5 of Part 2. Applications for membership are considered by EXCOM, to whom the LME Board of Directors has delegated authority to consider such applications. The applications are considered objectively against the criteria set out in the LME Rulebook at Part 2. If the LME decides not to admit a Candidate to Membership, it must notify him with a statement of reasons for the refusal and the Candidate may within 14 days of being notified of the Directors' decision lodge notice of appeal with the Secretary. Provisions for appeal to a single arbitrator are set out at Part 2 Regulation 5.8.

8 CLEARING AND SETTLEMENT

- 8.1 ***Clearing Arrangements – The exchange has appropriate arrangements for the clearing and settlement of transactions through a clearing house.***
- 8.1.1 Clearing services are provided to the LME by LME Clear. Each LME Clearing Member (Categories 1, 2 and 3) must also be a member of LME Clear. As such, the clearing arrangements for all LME Clearing Members (as required by LME Clear Rules and the specific terms of the participant agreement(s) between LME Clear and each Clearing Member) include requirements for the maintenance of appropriate bank accounts, payment facilities, documentation and the provision of collateral.
- 8.1.2 LME Clear is in the process of applying for an order exempting LME Clear from the requirement to be recognized by the OSC as a clearing agency under Section 21.2 of the OSA. Accordingly, subject to the above order being granted with respect to LME Clear, the appropriate arrangements that are regulated by the OSC would exist for the clearing and settlement of LME contracts.
- 8.2 ***Regulation of the Clearing House – The clearing house is subject to acceptable regulation.***
- 8.2.1 LME Clear is a limited company incorporated in England and is subject to the regulations of a clearing house recognized by the Bank. If LME Clear's application to become an exempt clearing organization in Ontario is granted, LME Clear will comply with the terms and conditions imposed by the OSC in its requested order, and compliance with these requirements are overseen by the OSC. As part of its oversight, the OSC reviews required filings and reviews any new substantive rules or substantive changes to current rules relating to access criteria, default management that are specific to the clearing services utilized by Ontario clearing members.
- 8.3 ***Authority of Regulator – A foreign regulator has the appropriate authority and procedures for oversight of the clearing house. This includes regular, periodic regulatory examinations of the clearing house by the foreign regulator.***
- 8.3.1 LME Clear is regulated in the UK as an approved CCP under Regulation (EU) No. 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (EMIR) and is subject to the FSMA. LME Clear is supervised by the Bank. Its authorisation was obtained on September 3, 2014.
- 8.3.2 The Bank is the responsible body for authorising and supervising CCPs in the UK. Under the EMIR regime, a College of European regulators (the College) is also formed to authorize and supervise the CCPs. The day to day supervision role is therefore delegated to the national regulator (being the Bank in the UK) but the authorization, as well as the extension of the authorization to include additional services or activities not covered by the initial authorization, must involve the College.

- 8.3.3 The Bank exercises its supervision of CCPs within the framework of the UK legal regime. Part 18 of FSMA is the main UK legislation relating to the regulation of CCPs. The standards that UK CCPs must meet to be recognized are set out in the Financial Services and Markets Act 2000 (Recognition Requirements for Investment Exchanges and Clearing Houses) Regulations. CCPs must continue to meet these standards to maintain their recognized status. The Bank oversees CCPs' continuing compliance with the recognition requirements. The UK legal regime sits within the applicable European Union regulations, being specifically EMIR, together with the related technical standards adopted by the European Securities and Markets Authority.
- 8.3.4 The Principles for Financial Market Infrastructures (**PFMIs**), published by the Committee on Payment and Market Infrastructure (**CPMI**) and the International Organization of Securities Commissions (**IOSCO**), form the keystone for the Bank's supervisory approach. The UK regulatory framework is therefore consistent with the minimum standards set out in the PFMIs.
- 8.4 **Access to the Clearing House**
- (a) *The clearing house has established appropriate written standards for access to its services.*
- (b) *The access standards for clearing members and the process for obtaining, limiting and denying access are fair, transparent and applied reasonably.*
- 8.4.1 The LME Clear Rules act as the master agreement between LME Clear and Members in respect of all transactions cleared by LME Clear. A copy of the current LME Clear Rules can be found at:
<http://lme.com/~media/Files/LME%20Clear/Rules%20and%20regulation/LME%20Clear%20Rules%20and%20Procedures%20CLEAN%20Published%20Version.pdf>
- 8.4.2 The application process for LME Clear is set out in Membership Procedure Part B of the LME Clear Rules and on the LME Clear section of the Website.
- 8.4.3 There are two categories of LME Clear Membership:
- (a) Individual Clearing Members (**ICMs**) are permitted to clear transactions on their own behalf only;
- (b) General Clearing Members (**GCMs**) may clear transactions on their own behalf and also in respect of transactions effected (i) by the GCM with its Clients or (ii) by its Clients with other non-Members.
- 8.4.4 There are no other participant types. Only Members, in their capacity of ICMs or GCMs, can set up accounts with LME Clear and access the system for clearing services. All Members are subject to the same Membership Criteria applicable to their membership category described under LME Clear Rule 3. Once admitted as Members, all Members have access to the same range of accounts and services as described in the LME Clear Rules. There are no clearing privileges available to some Members only.
- 8.5 ***Sophistication of Technology of Clearing House – The exchange has assured itself that the information technology used by the clearing house has been adequately reviewed and tested and provides at least the same level of safeguards as required of the exchange.***
- 8.5.1 LME Clear applies industry best practice for development, implementation, operations, monitoring, management and maintenance of IT systems, using industry standard hardware and processes for which experienced resources are readily available. LME Clear ensures that a bi-annual ITIL assessment review is completed by its key IT providers. The Chief Technology Officer is responsible for ensuring IT standards are applied. At the highest level, the IT standards adopted are:
- (a) new system development and project management: system development lifecycle model supported by formal project management methodology when developing large business components; and
- (b) IT Support Services: ITIL.
- 8.5.2 LME Clear has two key categories for changes that occur on its systems. These categories are Business As Usual (**BAU**) change and major releases.
- 8.5.3 BAU change encompasses minor patches and small works to the system. These changes can be in response to small works requested by the LME Clear business or patches required for incident and defect resolution. BAU changes are predominately internally facing with no or limited visibility to outside parties.

8.5.4 Major releases result in significant change to the system which may include impact to third parties.

Testing

8.5.5 Due to the differences in impact and visibility, the two change routes have different levels of testing and coordination applied to them. LME Clear aims to undertake two major releases per year, dependent upon business requirements. These changes are generally considered large scale in their nature with significant Member and external impact. Due to the size of these releases extensive testing is applied to each release, testing of a release is undertaken by LME Clear test and business teams. This ensures that LME Clear fully reviews all releases to ensure that they are of sufficient quality and stability for deployment into production.

8.5.6 Testing of a major release includes: Unit Testing, Functional Testing, User Acceptance Testing, Non-functional Testing, Regression Testing, Parallel Runs, Member Tests and Penetration Testing.

- (a) Unit testing is undertaken on all new code developed on the system. This is the first test applied and is undertaken by the developers of the code. This ensures that the code is good and addresses the core requirements it is intended for. If the code passes this test then it is promoted to the release for delivery to the LME Clear test team.
- (b) Functional Testing is applied to all new releases and patches. This testing ensures that the new release or patch functionally works as expected. The functional testing is done against detailed test plans that are created prior to the code delivery. This allows the testers to execute a wide number of tests and compare against expected outcomes. If a defect is identified then it is raised with the developers for correction either via a patch or a subsequent release. All defects are tracked and reported on as part of the release project governance.
- (c) User Acceptance Testing is undertaken by the LME Clear business teams on each element of the release. This test ensures that the LME Clear business confirms that they are able to undertake their required actions and activities on the system. If a defect is identified then it is raised with the developer for correction.
- (d) Regression testing is undertaken on all major releases. This test runs through a detailed risk based regression test pack. The pack covers key elements of the LME Clear activities to ensure all elements, regardless of whether they are being changed or not still function as expected. This test ensures that there are no unintended consequences of changes made to the system.
- (e) Member Tests are carried out with LME Clear's external members. This is done with the use of two dedicated Member test systems which are available to all LME Clear members. The Member test environments are setup to provide members with the ability to test against current state and future state. During a major release members are required to self-certify that they have tested against the new release.
- (f) Non-Functional Testing is applied to all releases. This test is focused on performance of the system with the new release. The test ensures that the system continues to perform with required trade volumes. These trade volumes include peak LME trade volume and 3x peak volume as required by EMIR. Non-functional tests also include failover and resilience testing which ensures that the system continues to meet the EMIR regulatory requirement of a 2 hour recovery period.
- (g) Parallel Run Tests are undertaken on all major releases. This test involves the pre-production system being run behind the production system with all trades and price updates experienced in production played into the test system. This test is carried out by the LME Clear business team and ensures that the system continues to provide the same results as production and that functionality is as expected by the business teams.
- (h) Penetration testing is undertaken on each new release. This is undertaken by a third party on LME Clear's behalf to ensure that there are no security flaws within the new release. If a severe security flaw is detected then this is corrected before go live of the release.

8.5.7 BAU changes are smaller in scope to the major releases and are delivered as patches to the system. This means that the changes are discreet in nature and can easily be removed if required. As a result of this, BAU changes undergo Unit Testing, Functional Testing and pre-production deployment testing before deployment into production.

8.5.8 LME Clear's COO and CTO meet regularly with the Bank and inform it of major releases planned and the expected go-live dates of these. BAU changes are made with no regulatory consultation.

8.6 ***Risk Management of Clearing House – The exchange has assured itself that the clearing house has established appropriate risk management policies and procedures, contingency plans, default procedures and internal controls***

8.6.1 Clearing services are provided by LME Clear and the relationship is governed by the Clearing Services Agreement. Please see paragraph 8.3.1 above for a description of LME Clear's regulatory status and its supervision by the Bank.

ERM Framework

8.6.2 LME Clear operates a comprehensive Enterprise Risk Management (**ERM**) framework. The approach to capture all risks is twofold; a top-down management led assessment of risks for each of the risk types identified in the Risk Appetite Statement and also a 'bottom-up' process led approach through the Operational Risk Management Policy that ensures all operational risks are identified and mapped against the key risk types. This provides a full picture of the risks to which LME Clear is exposed and allows for the measurement, monitoring and management of these risks.

8.6.3 The management of each of the risk types is assigned to a member of the extended Management Team within LME Clear as the first line. The operational risks are assessed on an ongoing basis and are the subject of a dedicated resource to ensure comprehensive coverage and to identify trends and solutions. The ERM is updated on an ongoing basis and is subject to formal review by the EXCOM and the Audit Committee on at least a quarterly basis.

Risk Appetite Statement

8.6.4 The Risk Appetite Statement lays out how the Board wishes to manage risk; this includes details of policy review cycles and the need to review each policy at least annually. In addition, the Board Risk Committee or Audit Committee (as the case may be) receives quarterly reporting on each of the policies and performance. In addition, the EXCOM receives monthly reporting on operational issues and reporting on performance.

8.6.5 The Audit Committee is responsible for (amongst other things):

- (a) Monitoring and reviewing the effectiveness of internal controls
- (b) Enterprise Risk Management
- (c) Operational Risk

Risk Models

8.6.6 LME Clear conducts an independent review of all of its models that are used as part of its day-to-day risk management. The review process encompasses a theoretical review and assessment of the model methodology including:

- (a) model and methodology coverage;
- (b) theoretical properties and assumptions underlying the models;
- (c) the adequacy of the models for their underlying products and markets and the purpose for which they were developed; and
- (d) the theoretical conditions under which model assumptions may be violated and result in a potential understatement of risk.

8.6.7 Validation testing is also performed to ensure that:

- (a) the model has been correctly and comprehensively tested and assessed;
- (b) the model produces results that are aligned to expectations under the test scenarios and validation procedures that have been performed;
- (c) the model has been tested over a sufficiently long history and range of market regimes and appropriate environments; and
- (d) the adequacy and appropriateness of the validation methodology and testing.

- 8.6.8 Risk policies are reviewed at least on an annual basis. All material changes to the underlying model or methodologies, liquidity risk framework, policies or the validation process require independent validation, advice from the Board Risk Committee and approval from the Bank.

9 SYSTEMS AND TECHNOLOGY

- 9.1 ***Systems and Technology – Each of the exchange’s critical systems has appropriate internal controls to ensure completeness, accuracy, integrity and security of information, and, in addition, has sufficient capacity and business continuity plans to enable the exchange to properly carry on its business. Critical systems are those that support the following functions:***

- (a) ***order entry,***
- (b) ***order routing,***
- (c) ***execution,***
- (d) ***trade reporting,***
- (e) ***trade comparison,***
- (f) ***data feeds,***
- (g) ***market surveillance,***
- (h) ***trade clearing, and***
- (i) ***financial reporting.***

Description of the matching system

- 9.1.1 LMEselect uses the TRADExpress platform owned by Cinnober Financial Technology AB. We understand this platform is widely used by various multinational exchanges throughout the world, including several exchanges that are headquartered in the United States. LMEselect is a customised version of this platform. This customisation is primarily required to tailor the platform to suit the LME’s unique daily Prompt Date structure.
- 9.1.2 A comprehensive description of how Members may connect to LMEselect is set out in the connectivity guide which is attached at Annex 2. There are two primary methods of access: (i) via a graphical user interface (**GUI**); and (ii) by way of the FIX API, which Members use to develop an interface between their in-house systems and LMEselect. The FIX API interface permits Members to route orders from their in-house systems to LMEselect. In addition to this, a number of independent software vendors (**ISVs**) offer off-the-shelf software solutions to members using the FIX API. Members and ISVs must have entered into software licences with LME prior to accessing LMEselect.
- 9.1.3 As non-Members of LME cannot have direct access to LMEselect, trades will always be routed through a Member and the counterparty risk to non-members will always be carried by a Clearing Member. This principle is imposed on the two primary forms of access to LMEselect as follows:
- (a) GUI: Any trader using the GUI to access LMEselect must be an accredited user. Each accredited user of LMEselect must be an employee of a Member or a person authorized by the FCA to trade on behalf of that Member; customers of Members cannot access LMEselect via the GUI. Once authorized, each accredited user is given a unique user login that is the responsibility of the Member to maintain. Each Member must ensure that necessary and proportionate pre and post-trade risk controls are in place with regards to use of GUI and certain functionality of the GUI may be customised such that use of the GUI can be restricted or limited for a particular user.
 - (b) FIX API: Where a Member wishes to access LMEselect via the FIX API, it will submit a request for a FIX key to LME. As a client of a Member is able to order route its trades via a Member into LMEselect, each request for a FIX key must specify who will access LMEselect via that FIX key. Each Member must ensure that any necessary and proportionate pre and post-trade risk controls are in place with regards to access using the FIX key. It is the responsibility of the Member to notify LME of any change of user associated with a particular FIX key. Members must ensure that a tag field is populated within LMEselect with a code produced by the Member’s own system that will identify a client. LME’s Market Operations department is able to identify which

Member or client account is represented by that code. This condition of access enables the LME to monitor order routing through the FIX API.

- 9.1.4 Irrespective of the means of access to LMEselect, Members are responsible for ensuring that all activity on LMEselect is conducted in accordance with the LME Rules and with all other applicable regulatory requirements. A Member to which a GUI login or FIX key is provided is responsible for all activity in relation to that GUI login or FIX key, including ensuring that necessary and proportionate pre and post-trade risk controls are in place. In the case of a FIX key, this applies irrespective of whether a Member or client account is trading through that FIX key. Members are financially accountable for any trading activity undertaken on LMEselect via a GUI log-in or FIX key in their name and may be subject to disciplinary action, if such Member fails to ensure compliance with the LME Rules.
- 9.1.5 In respect of all other overseas regulatory relationships (US CFTC, Australia ASIC, Hong Kong SFC, Singapore MAS), the GUI is considered the only method of direct access to the LME's trading system, and therefore the volume generated on LMEselect by individuals who are notified to the Exchange as having access through the GUI from the relevant jurisdiction (i.e. US, Australia, Hong Kong, Singapore) is the volume we report to the relevant regulator. So for example in the US we report all participants who have access to the GUI from the US (i.e. who are physically located in the US) as "US Participants" but we do not report participants who have access via the API because they are not accessing the LME's systems directly (they are using their own systems to access the market). In the same way, we would propose to report any individuals who are physically located in Ontario and accessing the GUI as "Ontario Participants" for the purposes of paragraph 20(g)(i) and (ii) of the terms and conditions of the draft exemption order.

Description of the architecture of the systems, including hardware and distribution network, as well as any pre- and post-trade risk-management controls

- 9.1.6 The FCA considers the LME's pre-trade and post-trade systems and controls to comply with the requirements of ESMA's "Guidelines on systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities" issued in December 2011. LME's pre and post-trade risk management controls are well aligned to the business which takes place through its markets and are robust enough to ensure continuity and regularity in the performance of these markets. The LME's pre and post-trade risk management controls include:
- (a) Order to trade ratio: LME's order to trade ratio policy has been designed to ensure orderly conduct of trading on LMEselect and to protect LME and Member systems. It applies to each individual market participant (Member user or Member client, identified by the unique client identifier code via FIX order entry and the LMEselect GUI user name) that enters 50,000 or more orders on a trading day between 00:45 and 19:00. The policy stipulates that a fee of £10,000 will be charged to the relevant Member in respect of any LMEselect FIX client or GUI user that exceeds a ratio of orders to lots generated of 50:1 as an average via a single FIX key or aggregate across two or more FIX keys during a trading day (00:45 - 19:00). The Exchange will waive the fee for the first event each month. It should be noted that the LME reserves the right to restrict or suspend access to LMEselect if the LME determines in its absolute discretion that the message usage generated from any LMEselect order routing client, GUI user or from any Member connection becomes capable of impairing the orderly conduct of trading on LMEselect.
 - (b) Trade cancellation: The LMEselect Error Trade Policy came into effect on 15th February, 2016. The LME's Policy for the treatment of orders that have been executed at prices not representative of the market is to generally adjust the price of an error trade rather than invalidate it. The Policy includes 'No Cancellation Ranges' (NCR) and any erroneous trade is subject to price adjustment using the full range of the NCR. The Policy includes the ability to invalidate transactions where the LME determines, in its absolute discretion, that it would be more appropriate for the market if the transactions in question were invalidated.
 - (c) Throttling policy: The maximum number of order or entries updates that can take place on LMEselect is 40 per second for each LMEselect FIX key. Order or entry updates submitted in excess of this in any given second will be queued and smoothed over the following seconds according to the throttling limit maximum. Order or entry updates are not rejected.
 - (d) User-level permissions: The trading ability of each GUI or FIX key user can be restricted so that only a certain type or types of contract can be traded. Members can also set bespoke volume and price deviation limits for each user.
 - (e) Volume and price limiting functionality: LME sets hard limits for the maximum order volume. For price limiting LME uses a dynamic price banding mechanism to constrain the allowable prices accepted on new or modified orders. This mechanism dynamically calculates a price reference curve and configurable price bands are applied to control the permitted order price. These dynamic price band limits are constantly monitored to

ensure that they are set at appropriate levels with reference to the market at that time. These levels are publicly available so that all LMEselect users are aware of the limits at any given time.

- (f) In April 2014 LME introduced pre-trade risk management (**PTRM**) functionality to LMEselect. As well as enabling a more secure market for all, PTRM provides greater visibility when onboarding new clients. More specifically, PTRM provides Members with the ability to set limits for their own trader users and order-routing clients. All orders sent to the LMEselect system pass through this pre-trade risk system regardless of whether specific limits have been set for a particular user account or not.

9.1.7 LME stays abreast of technological advancements and trends in the use of technology by its members and their clients by liaising directly with other exchanges and attending and participating in industry working groups and roundtable events. In line with the implementation of MiFID II, the LME has introduced additional pre and post-trade risk controls including dynamic price limits and an interval price limit (automated circuit breaker).

9.1.8 Members and ISVs may also add additional pre and post-trade risk management functionality to the trading systems that are used to connect to LMEselect via the FIX API. The GUI also has certain in-built controls as set out in the LMEselect user guide.

Market continuity provision

9.1.9 For the LME, any stoppages that may occur are mitigated by the failover to its parallel markets: the telephone market and the Ring. As a result, any interruptions that may occur to LMEselect are less significant than those faced by purely electronic exchanges given that trading can continue on these parallel markets.

9.1.10 In 2017 the availability of LMEselect was 99.76% during its trading hours. LME has in place robust contractual arrangements with its third party service providers to ensure extremely high availability of its entire core IT infrastructure.

9.1.11 LME has detailed business continuity and disaster recovery plans and procedures for all of its business operations. The FCA regularly reviews LME's business continuity and disaster recovery procedures. LMEselect has a highly available design architecture that includes a dual data centre failover capability. If there is a fault with the primary data centre where LMEselect is hosted, the secondary data centre will be utilised. These installations replicate each other in real time so that the trading information on both is up to date at all times. LME routinely validates this failover capability to ensure continued service if there is a fault. Disaster Recovery Tests of all services are performed annually.

9.1.12 Members who access LMEselect are recommended to have two network lines diversely routed using the LMEselect service provided by COLT Technology Services in order to ensure resilient connectivity to LMEselect.

9.1.13 All LMEselect system data is backed up on a daily basis and stored off site; additionally, LMEselect current data is housed in two geographically separate data centres which are synchronised in real-time, providing a real-time backup of critical data.

9.2 *Information Technology Risk Management Procedures – The exchange has appropriate risk management procedures in place including those that handle trading errors, trading halts and circuit breakers.*

9.2.1 Under REC, the LME must always be able to take any reasonable step to “ensure that business conducted by means of its facilities is conducted in an orderly manner and so as to afford proper protection to investors.” In particular, the guidance in REC 2.6.29 (3) confirms that the FCA will have regard to whether the LME's arrangements and practices “include procedures which enable [it] to influence trading conditions or suspend trading promptly when necessary to maintain an orderly market”.

9.2.2 The LME takes steps to ensure that a fair and orderly market is maintained with regard to the submission of orders, and to protect both the LME and Members' own systems and infrastructure from inappropriate activity. The LME performs ongoing monitoring of the LMEselect, including, without limitation, performance and capacity, orders sent by Members on an individual and aggregated basis, message flow, and the concentration flow of orders, to detect potential threats to the orderly functioning of the market.

9.2.3 In addition to measures stated in paragraph 9.1, the LME has arrangements to prevent disorderly trading and breaches of capacity limits:

- (a) throttle limit, which limits the maximum number of order entries/updates sent per Member per second;

- (b) mechanisms to manage volatility; and
- (c) pre-trade controls.

9.2.4 The dynamic price band functionality enables the LME to manage volatility which may include, where appropriate, the temporary suspension of the matching of orders in LMEselect. The LME may, at its absolute discretion, acting reasonably, suspend trading on LMEselect for such periods it considers necessary in the interests of maintain a fair and orderly market. The LME will keep such suspension under constant review, and trading will be resumed as soon as reasonably practicable following any such suspension of LMEselect.

9.2.5 The LME may suspend access to LMEselect or any of its systems, either at the individual Member or dealer level or for the whole market. This action may be taken at the initiative of the LME or at the request of the relevant Member or where required by the LME Clear Rules, or by the FCA or any other relevant regulatory authority.

Trade Halts

9.2.6 The 'kill switch' or 'trade halt' is a feature of the LME's Pre Trade Risk Management functionality and enables relevant staff in Trading Operations to halt trading across the market as a whole, in a particular contract, a prompt date of a contract, or access to trading by individual users in LMEselect.

9.2.7 A trade halt can be applied by Trading Operations if LMEselect is experiencing one of the following issues:

- (a) Network or technical issues;
- (b) Incorrect uploaded reference data;
- (c) Any other scenario when a trade halt would be deemed to be in the best interests of the market.

9.2.8 The decision to apply a trade halt must be authorised by two members of EXCOM and recorded. In the event that the underlying of a derivative has been suspended, any related derivative that is completely dependent on the former must also be suspended. An example of this is an option that is linked to a derivative whose underlying has been suspended.

Error Trades

9.2.9 For every LME contract, the LME will specify a no-cancellation range (NCR) which is published on the website. This governs the price range in which the LME deems a trade acceptably-priced, or not acceptably-priced. The Error Trade Policy (please see Ref 17/344 - Appendix 1 at <https://www.lme.com/About/Regulation/Rules/Notices>) sets out the following circumstances:

- (a) the NCR which Members are not permitted to cancel error trades;
- (b) the LME permits cancellation of error trades outside the NCR where both parties agree to cancel; and
- (c) the LME may price-adjust the rate of the trade, rather than invalidate it.

9.2.10 The LME Order Cancellations and Controls Policy can be found at Appendix 3 of Notice 17/344 which is available at <https://www.lme.com/About/Regulation/Rules/Notices>. Paragraph 10 of this policy refers to the LME's throttle limit per user, which limits the number of order entries and updates to 40 per second.

Members' Controls

9.2.11 The LME Rules require Members to comply with all relevant regulatory requirements including, but not limited to, those set out in MiFID II. In particular Members must have policies in place for the following:

- (a) Pre-trade controls on price, volume, value and usage of LMEselect, and post-trade controls on the Member's trading activities across both LMEselect and the Matching System;
- (b) these policies should set out the process by which the configuration for each control is determined; the process for revising such configuration, and any over-ride or emergency process;
- (c) the technical and functional conformance testing that must be undertaken prior to deployment of all third-party systems and/or applications that interface with LMEselect and/or the Matching System.

- (d) in addition to any over-ride or emergency policy referred to in b) above, Members must have a policy relating to the use of kill functionality with regard to business executed on LMEselect.

9.2.12 Members must ensure that the above policies are also reflected in relevant “Business Continuity/Disaster Recovery Plans” maintained and followed by Members, such that the invocation of either does not result in any reduction in the level of control exercised over the business conducted through the LME’s systems. Members must ensure that all staff in key positions at Members are suitably qualified.

10 FINANCIAL VIABILITY AND REPORTING

10.1 ***Financial Viability – The exchange has sufficient financial resources for the proper performance of its functions and to meet its responsibilities.***

10.1.1 The FSMA Recognition Requirements specify that the LME must have financial resources sufficient for the proper performance of its functions as an RIE. In considering whether this requirement is satisfied, the FCA must take into account all the circumstances, including the LME’s connection with any person, and any activity carried on by LME, whether or not it is an exempt activity.

10.1.2 The FCA has adopted guidance in the FCA Handbook at REC 2.3 which elaborates on the FSMA Recognition Requirements. This guidance sets out principles which the FCA will take into account to determine if the above requirement has been satisfied. This guidance states that a UK RIE which at any time holds:

- (a) eligible financial resources not less than the greater of:
 - (i) an amount calculated under the standard approach (equal to six months of operating costs); and
 - (ii) an amount calculated under a risk-based approach (which involves the undertaking of an annual financial risk assessment); and
- (b) net capital not less than the amount eligible financial resources determined under (a);

will, at the time, be considered to have sufficient financial resources in respect of operational and other risks unless there are special circumstances indicating otherwise.

10.1.3 LME maintains the current minimum capital amounts needed, and will maintain any future minimum capital amounts needed to meet FCA requirements.

11 TRANSPARENCY

11.1 ***Transparency – The Exchange has adequate arrangements to record and publish accurate and timely trade and order information. This information is provided to all participants on an equitable basis.***

11.1.1 The LME complies with the relevant MiFID II Regulatory Technical Specifications on pre- and post-trade transparency requirements. The LME Rules describe sound trading practices and the accuracy of market information provided by participants to ensure the transparency of market behavior of all market participants.

11.1.2 The LME’s Real Time Market Data feed (**LMEselectMD**) provides detailed, real-time, historic and summary reports of trading activity within LME for external data vendors and market participants. The system is supported on a 24x5 basis and is fundamental to the operation of the LME and the market. The data feed is monitored by IT to detect any potential disruption to the provision of the data, which would be investigated and resolved.

11.1.3 The commercial terms for market data apply in a non-discriminatory way and are published on the LME website and via notice. Information on the fee schedule more widely is also publically available. The Market Data model has been built to reflect MIFID II requirements on publication of pre- and post-trade data.

Pre-trade Publication

11.1.4 Bids and offers made via open outcry in the Ring are captured by LME’s Trading Operations team and published to the market via LMEselect MD. All orders submitted to LMEselect (the LME’s electronic order book), are published on a near real-time basis via LMEselect MD, the LME’s market data feed. Every half trade instruction that is submitted to the LME’s matching system (**LMEsmart**) on the inter-office market is published on a near real-time basis via LMEselect MD.

Post-trade Publication

- 11.1.5 Where orders match in LMEselect so the resulting trades are published to the market on a near real-time basis via LMEselect MD. Trades executed via open outcry in the Ring are captured by LME's Trading Operations team and published to the market via LMEselect MD. Half-trade instructions matched on the inter-office market are then published on near real-time on LMEselect MD.

12 RECORD KEEPING

- 12.1 ***Record Keeping – The exchange has and maintains adequate systems in place for the keeping of books and records, including, but not limited to, those concerning the operations of the exchange, audit trail information on all trades, and compliance with, and/or violations of exchange requirements.***

- 12.1.1 MiFID imposes a broad obligation upon investment firms to retain records for a minimum of five years. The FCA Handbook requires authorized firms to retain certain records for longer periods.

- 12.1.2 All persons that have been authorized to conduct investment business in the UK are subject to the audit trail and conduct of business rules imposed by the FCA. FCA authorized firms are required to maintain records of any written communication between the firm and its customers concerning regulated business and to retain copies of contract notes, confirmation notes, and exercise notices.

- 12.1.3 LME Rules set forth similar audit trail requirements – see for example regulation 9.6 of Part 2 of the LME Rules in particular. All dealings by Members must be properly documented and then reconciled with LME Clear. For every contract traded, Members must use a specific code indicating the nature of each transaction. Additionally, the LME's IT infrastructure ensures that all material information regarding: (i) the activity of LME participants; (ii) all orders placed, varied or cancelled by Members; and (iii) all transactions executed by Members, is recorded, processed and stored in a manner that enables the information to be reviewed by LME and other entities that have a regulatory interest in the information. Regulation 9 of Part 2 of the LME Rules requires Members to permit access to their premises and to relevant records; the Member surveillance team exercises these powers during its audit program. In addition pursuant to Regulation 9 of Part 2 of the LME Rules, Members are required to forward information about their activity to LME, and procure their clients to do the same, upon request.

- 12.1.4 All relevant data relating to orders and trades is captured in LMEselect. This information can be exported by appropriately authorized Member users and LME users of LMEselect and therefore retained indefinitely.

- 12.1.5 The LME has a detailed record retention policy which details how all relevant records must be kept, and for how long. This ensures that the LME remains in compliance with all relevant regulatory requirements, which include REC and also relevant UK and European data protection requirements (including the UK Data Protection Act and the forthcoming General Data Protection Regulation or "GDPR").

13 OUTSOURCING

Outsourcing – Where the Exchange has outsourced any of its key services or systems to a service provider, it has appropriate and formal arrangements and processes in place that permit it to meet its obligations, and that are in accordance with industry best practices.

The LME does not outsource any of its key services or systems.

14 FEES

14.1 Fees

(a) ***All fees imposed by the exchange are reasonable and equitably allocated and do not have the effect of creating unreasonable condition or limit on access by participants to the services offered by the exchange.***

(b) ***The process for setting fees is fair and appropriate, and the fee model is transparent.***

- 14.1.1 The LME's fees are set out on the website at <https://www.lme.com/Trading/Access-the-market/Fees>. The LME's fees have been designed to be fair, transparent and non-discriminatory, as required by applicable legislation, including the Recognition Requirements and MiFID II.

- 14.1.2 There are two types of contracts traded on the LME – Cleared Contracts and Client Contracts. A Cleared Contract is a contract agreed between two Clearing Members of the LME (Categories 1-3) and a Client Contract is a contract agreed between a Client and a Category 1, 2, or 4 Member. The LME operates three trading venues, the Ring, the inter-office market and LMEselect. All Member-to-Member trades and Client trades executed on any of the three venues are submitted to the LME matching system, LMEsmart, for matching and registration. All trades entered into LMEsmart are then automatically transmitted to the clearing system, LMEmercury.
- 14.1.3 EDW houses the LME fee calculator. The LME Fee calculator assigns each trade a transaction fee according to certain criteria, i.e. whether it is a Member-to-Member or Client trade, an outright, long-dated, medium dated or short-dated carry, a Ring, Basis Ring, Inter-Office or Select trade, or a Give-Up trade. All fees imposed by the exchange are reasonable and equitably allocated and do not have the effect of creating unreasonable conditions or limiting access by participants to the services offered by the exchange.
- 14.1.4 The LME's fees are set by the Board. In setting fees, the LME takes into account the fees charged by competitors for equivalent transactions to ensure that fees are fair and non-discriminatory.

15 INFORMATION SHARING AND OVERSIGHT ARRANGEMENTS

15.1 *Information Sharing and Regulatory Cooperation – The exchange has mechanisms in place to enable it to share information and otherwise co-operate with the OSC, self-regulatory organizations, other exchanges, clearing agencies, investor protection funds, and other appropriate regulatory bodies.*

- 15.1.1 The Chief Executive of LME warrants to notify OSC staff promptly if any of the representations made in connection with or related to this application for LME's registration cease to be true or correct in any material respect, or become incomplete or misleading.
- 15.1.2 Additional information relevant to LME, LMEselect and market participants will be available to the OSC and its staff through the OSC-FCA MOU.
- 15.1.3 LME Clear does not have any existing arrangements in place with the OSC but has applied for an order seeking exemption from the requirements to be recognized as a clearing agency in Ontario and thus it is expected that, if the order is granted, as part of its terms and conditions, there will be appropriate reporting requirements prescribed by the OSC.
- 15.1.4 The FCA is party to the IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information, as is the OSC.
- 15.1.5 The FCA is party to the Declaration on Cooperation and Supervision of International Futures Exchanges and Clearing Organizations.

15.2 *Oversight Arrangements – Satisfactory information sharing and oversight agreements exist between the Ontario Securities Commission and the Foreign Regulator.*

- 15.2.1 The OSC, together with the Autorité des marchés financiers, Alberta Securities Commission and British Columbia Securities Commission, have entered into a Memorandum of Understanding with the Bank and FCA concerning regulatory cooperation related to the supervision and oversight of regulated entities that operate in both the UK and Canada (the **Supervisory MOU**). The Supervisory MOU provides a comprehensive framework for consultation, cooperation and information-sharing related to the day-to-day supervision and oversight of cross-border regulated entities and enhances the OSC's ability to supervise these entities. The Supervisory MOU became effective on August 21, 2013.

16 IOSCO PRINCIPLES

16.1 *IOSCO Principles – To the extent it is consistent with the laws of the foreign jurisdiction, the exchange adheres to the standards of the International Organization of Securities Commissions (IOSCO) including those set out in the "Principles for the Regulation and Supervision of Commodity Derivatives Markets" (2011).*

- 16.1.1 The LME adheres to the IOSCO principles by virtue of the fact that it must comply with the FCA rules and regulations, which reflect the IOSCO standards. The UK was on the working group that developed these Principles and the predecessor organization to the FCA (the FSA) endorsed them.

- 16.1.2 The LME adheres to the IOSCO principles set out in the “Objectives and Principles of Securities Regulation” (2003) applicable to exchanges and trading systems. The LME maintains operations to achieve the following and works closely with LME Clear to:
- (a) ensure the integrity of trading through fair and equitable rules that strike an appropriate balance between the demands of different market participants;
 - (b) promote transparency of trading;
 - (c) detect and deter manipulation and other unfair trading practices;
 - (d) ensure proper management of large exposures, default risk and market disruption; and
 - (e) ensure that clearing and settlement of transactions are fair, effective and efficient, and that they reduce systemic risk.

Part III Submissions by LME

1. Submissions Concerning the Exchange Relief

- A. All contracts traded on the LME fall under the definitions of “commodity futures contract” or “commodity futures option” set out in section 1 of the CFA. The LME is therefore considered a “commodity futures exchange” as defined in section 1 of the CFA and is prohibited from carrying on business in Ontario unless it is registered or exempt from registration under section 15 of the CFA. LME seeks to provide Ontario market participants with direct, electronic access to trading in LME contracts and may therefore be considered to be “carrying on business as a commodity futures exchange” in Ontario.
- B. LME is not registered with or recognized by the OSC as a commodity futures exchange under the CFA and no LME contracts have been accepted by the Director (as defined in the OSA) under the CFA. Therefore, LME contracts are considered “securities” under paragraph (p) of the definition of “security” set out in subsection 1(1) of the OSA and the LME is considered an “Exchange” under the OSA. Therefore, LME is prohibited from carrying on business in Ontario unless it is recognized or exempt from recognition under subsection 21(1) of the OSA. The LME seeks to provide Ontario market participants with direct, electronic access to trading in LME contracts and may therefore be considered to be “carrying on business as an Exchange” in Ontario.
- C. LME satisfies all the criteria for registration or exemption from registration as a commodity futures exchange and recognition or exemption from recognition as an exchange set out by OSC Staff, as described under Part II of this application. Ontario market participants that trade in commodity futures would benefit from the ability to trade on the LME, as they would have access to a range of exchange-traded metal products which are not currently available in Ontario. The LME would offer its Ontario Participants a transparent, efficient and liquid market to trade LME contracts. LME uses sophisticated information systems and has adopted rules and compliance functions that will ensure that Ontario users are adequately protected in accordance with international standards set by IOSCO. We therefore submit that it would not be prejudicial to the public interest to grant the Requested Relief.
- D. Provided that the OSC exempts LME from the requirement to be registered as a commodity futures exchange under the CFA, LME will be an “exempt exchange” as defined in OSC Rule 91-503 *Trades in Commodity Futures Contracts and Commodity Futures Options Entered into on Commodity Futures Exchanges Situate Outside of Ontario (OSC Rule 91-503)* and the LME contracts will be “exempt exchange contracts” under OSC Rule 91-503. We submit that OSC Rule 91-503 applies to the LME as the LME is “situated outside Ontario” and that separate exemptive relief for trades in LME contracts is not required from the registration requirement in Section 25 of the OSA and prospectus requirement in section 53 of the OSA pursuant to Part II of OSC Rule 91-503.

2. Submissions Concerning the Hedger Relief

- A. LME seeks to provide direct access to trading on the LME by Ontario Participants that may be “hedgers” as defined in subsection 1(1) of the CFA. Section 32(1)(a) of the CFA provides an exemption from registration for trades “by a hedger through a dealer,” which will not be available to Ontario resident hedgers because they will have direct access to LME and will not be considered to be executing “through a dealer”.
- B. To become Members, Ontario Participants must comply with the LME Rules and all applicable law pertaining to the use of LME. As well, the relevant LME Clear Member with which an Ontario Participant seeks to open an account for the purpose of trading on LME will complete credit, know-your-client and anti-money laundering checks, suitability analyses and other account supervision procedures prior to entering into clearing agreements with all clients and on an ongoing

basis in accordance with FCA and LME requirements. Furthermore, because the LME Clear Members are ultimately responsible for the trading activity of any Ontario Participants that they agree to guarantee, they can be expected to ensure that they themselves, and other such Ontario Participants, will have the regulatory permissions, requisite sophistication, and proficiency in the trading of LME contracts to satisfy investor protection concerns associated with having direct access to the LME.

- C. LME intends to confirm that Ontario Participants that seek to rely on the Hedger Relief are “hedgers” (as defined in subsection 1(1) of the CFA) by obtaining a representation stating such from the Ontario resident hedgers as part of their onboarding documentation. The documentation will specify that this representation is deemed to be repeated by the Ontario Participant each time it enters an order for a contract on the LME and that the Ontario Participant must be a “hedger” for the purposes of each trade resulting from such an order.
- D. The requested Hedger Relief will allow sophisticated Ontario residents who meet the definition of “hedger” to become Ontario Participants and gain the benefits of direct access to the LME. Given the sophistication of such Ontario Participants and the fact that the financial responsibility for their trading activity ultimately lies with the LME Clearing Member that guarantees their trades, it is not necessary for the protection of other investors or the integrity of the market to require such Ontario Participants to trade in LME contracts through a dealer rather than having direct access to LME.

3. Submissions Concerning the Bank Relief

- A. Section 35.1 of the OSA (the **Section 35.1 Exemption**) provides that financial institutions, such as Ontario Banks, are exempt from the requirement to be registered under the OSA to act as dealers provided that the conditions of the exemption are met. However, there is no corresponding exemption from registration for trades by financial institutions, such as Ontario Banks, in the CFA. For this reason, the LME is seeking the OSC’s approval for the Bank Relief.
- B. The LME intends to confirm that Ontario Participants that seek to rely on the Bank Relief are banks listed in Schedule 1 to the *Bank Act* (Canada), or are otherwise exempt from the requirement to be registered in Ontario, by obtaining a representation from the Ontario resident applicants for membership in their onboarding documentation. The documentation will specify that this representation is deemed to be repeated by the Ontario Participant each time it enters an order for a contract on the LME.
- C. The Registration Relief will allow sophisticated Ontario residents who are banks listed in Schedule 1 to the *Bank Act* (Canada) to become Ontario Participants and gain the benefits of direct access to the LME. Given the sophistication and heavy regulation of such Ontario Participants, it is not necessary for the protection of other investors or the integrity of the market to require such Ontario Participants to send their orders through a registered dealer rather than accessing the LME directly.
- D. If the Bank Relief is granted, it would suggest the OSC agrees that the policy basis that underlies the Section 35.1 Exemption from the dealer registration requirements of the OSA would also be a valid policy basis for an order exempting Ontario Banks from the dealer registration requirements under the CFA. As well, if the Exchange Relief is granted, the LME will be exempt from the requirements to be recognized as a stock exchange under the OSA and to be registered as an exchange under the CFA and the OSC will effectively be authorising the LME to carry on business as a commodity futures exchange in Ontario. The granting of the Exchange Relief would also mean that the LME has satisfied the OSC’s criteria for recognition (or exemption from recognition) of an exchange as set out in Staff Notice 21-702 and under the approval criteria discussed above. However, because the CFA does not contemplate that the OSC may exempt exchanges from its registration and/or recognition requirements, it does not include contracts traded on an exchange that has been exempted from the registration and/or recognition requirements as a category of “permitted contract” under Section 33 of the CFA. As a result, Ontario Participants will not be permitted to trade contracts on the LME even though (i) the LME would be authorized to carry on business in Ontario by virtue of the Exchange Relief being granted, and (ii) Ontario Banks would be exempt from the requirement to be registered as dealers under the CFA by virtue of the Bank Relief being granted. Since the LME expects its prospective participants will be Ontario Banks currently, as an extension of the above logic the LME requests the Bank Relief so that Ontario Banks that become Ontario Participants can trade contracts on the LME.

3. Similar Relief has been Granted

The LME notes that exemptive relief similar to the Requested Relief has been granted by the OSC in (i) *In the Matter of ICE Futures* (September 1, 2006), (ii) *In the Matter of Onechicago, LLC* (October 14, 2016), and (iii) *In the Matter of Nodal Exchange, LLC* (October 7, 2014).

Part IV Other Matters

LME consents to the publication of this Application for public comment in the OSC Bulletin.

Should you have any questions on this application, please contact the LME Legal team..

Yours faithfully,

LME

APPENDIX 1

CRITERIA FOR EXEMPTION

PART 1 REGULATION OF THE EXCHANGE

1.1 Regulation of the Exchange

The exchange is regulated in an appropriate manner in another jurisdiction by a foreign regulator (**Foreign Regulator**).

1.2 Authority of the Foreign Regulator

The Foreign Regulator has the appropriate authority and procedures for oversight of the exchange. This includes regular, periodic oversight reviews of the exchange by the Foreign Regulator.

PART 2 GOVERNANCE

2.1 Governance

The governance structure and governance arrangements of the exchange ensure:

- (a) effective oversight of the exchange,
- (b) that business and regulatory decisions are in keeping with its public interest mandate,
- (c) fair, meaningful and diverse representation on the board of directors (Board) and any committees of the Board, including:
 - (i) appropriate representation of independent directors, and
 - (ii) a proper balance among the interests of the different persons or companies using the services and facilities of the exchange,
- (d) the exchange has policies and procedures to appropriately identify and manage conflicts of interest, and
- (e) there are appropriate qualifications, remuneration, limitation of liability and indemnity provisions for directors, officers and employees of the exchange.

2.2 Fitness

The exchange has policies and procedures under which it will take reasonable steps, and has taken such reasonable steps, to ensure that each director and officer is a fit and proper person.

PART 3 REGULATION OF PRODUCTS

3.1 Review and Approval of Products

The products traded on the exchange and any changes thereto are reviewed by the Foreign Regulator, and are either approved by the Foreign Regulator or are subject to requirements established by the Foreign Regulator that must be met before implementation of a product or changes to a product.

3.2 Product Specifications

The terms and conditions of trading the products are in conformity with the usual commercial customs and practices for the trading of such products.

3.3 Risks Associated with Trading Products

The exchange maintains adequate provisions to measure, manage and mitigate the risks associated with trading products on the exchange including, but not limited to, margin requirements, intra-day margin calls, daily trading limits, price limits, position limits, and internal controls.

PART 4 ACCESS

4.1 Fair Access

- (a) The exchange has established appropriate written standards for access to its services including requirements to ensure
 - (i) participants are appropriately registered as applicable under Ontario securities laws or Ontario commodity futures laws, or exempted from these requirements,
 - (ii) the competence, integrity and authority of systems users, and
 - (iii) systems users are adequately supervised.
- (b) The access standards and the process for obtaining, limiting and denying access are fair, transparent and applied reasonably.
- (c) The exchange does not unreasonably prohibit, condition or limit access by a person or company to services offered by it.
- (d) The exchange does not
 - (i) permit unreasonable discrimination among participants, or
 - (ii) impose any burden on competition that is not reasonably necessary and appropriate.

PART 5 REGULATION OF PARTICIPANTS ON THE EXCHANGE

5.1 Regulation

The exchange has the authority, resources, capabilities, systems and processes to allow it to perform its regulation functions, whether directly or indirectly through a regulation services provider, including setting requirements governing the conduct of its participants, monitoring their conduct, and appropriately disciplining them for violations of exchange requirements.

PART 6 RULEMAKING

6.1 Purpose of Rules

- (a) The exchange has rules, policies and other similar instruments (Rules) that are designed to appropriately govern the operations and activities of participants.
- (b) The Rules are not contrary to the public interest and are designed to
 - (i) ensure compliance with applicable legislation,
 - (ii) prevent fraudulent and manipulative acts and practices,
 - (iii) promote just and equitable principles of trade,
 - (iv) foster co-operation and co-ordination with persons or companies engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in the products traded on the exchange,
 - (v) provide a framework for disciplinary and enforcement actions, and
 - (vi) ensure a fair and orderly market.

PART 7 DUE PROCESS

7.1 Due Process

For any decision made by the exchange that affects a participant, or an applicant to be a participant, including a decision in relation to access, exemptions, or discipline, the exchange ensures that:

- (a) parties are given an opportunity to be heard or make representations, and
- (b) it keeps a record of, gives reasons for, and provides for appeals or reviews of its decisions.

PART 8 CLEARING AND SETTLEMENT

8.1 Clearing Arrangements

The exchange has appropriate arrangements for the clearing and settlement of transactions through a clearing house.

8.2 Regulation of the Clearing House

The clearing house is subject to acceptable regulation.

8.3 Authority of Regulator

A foreign regulator has the appropriate authority and procedures for oversight of the clearing house. This includes regular, periodic regulatory examinations of the clearing house by the foreign regulator.

8.4 Access to the Clearing House

- (a) The clearing house has established appropriate written standards for access to its services.
- (b) The access standards for Clearing Members and the process for obtaining, limiting and denying access are fair, transparent and applied reasonably.

8.5 Sophistication of Technology of Clearing House

The exchange has assured itself that the information technology used by the clearing house has been adequately reviewed and tested and provides at least the same level of safeguards as required of the exchange.

8.6 Risk Management of Clearing House

The exchange has assured itself that the clearing house has established appropriate risk management policies and procedures, contingency plans, default procedures and internal controls.

PART 9 SYSTEMS AND TECHNOLOGY

9.1 Systems and Technology

Each of the exchange's critical systems has appropriate internal controls to ensure completeness, accuracy, integrity and security of information, and, in addition, has sufficient capacity and business continuity plans to enable the exchange to properly carry on its business. Critical systems are those that support the following functions:

- (a) order entry,
- (b) order routing,
- (c) execution,
- (d) trade reporting,
- (e) trade comparison,
- (f) data feeds,
- (g) market surveillance,
- (h) trade clearing, and
- (i) financial reporting.

9.2 Information Technology Risk Management Procedures

The exchange has appropriate risk management procedures in place including those that handle trading errors, trading halts and circuit breakers.

PART 10 FINANCIAL VIABILITY

10.1 Financial Viability

The exchange has sufficient financial resources for the proper performance of its functions and to meet its responsibilities.

PART 11 TRANSPARENCY

11.1 Transparency

The exchange has adequate arrangements to record and publish accurate and timely trade and order information. This information is provided to all participants on an equitable basis.

PART 12 RECORD KEEPING

12.1 Record Keeping

The exchange has and maintains adequate systems in place for the keeping of books and records, including, but not limited to, those concerning the operations of the exchange, audit trail information on all trades, and compliance with, and/or violations of exchange requirements.

PART 13 OUTSOURCING

13.1 Outsourcing

Where the exchange has outsourced any of its key services or systems to a service provider, it has appropriate and formal arrangements and processes in place that permit it to meet its obligations and that are in accordance with industry best practices.

PART 14 FEES

14.1 Fees

- (a) All fees imposed by the exchange are reasonable and equitably allocated and do not have the effect of creating an unreasonable condition or limit on access by participants to the services offered by the exchange.
- (b) The process for setting fees is fair and appropriate, and the fee model is transparent.

PART 15 INFORMATION SHARING AND OVERSIGHT ARRANGEMENTS

15.1 Information Sharing and Regulatory Cooperation

The exchange has mechanisms in place to enable it to share information and otherwise co-operate with the Commission, self-regulatory organizations, other exchanges, clearing agencies, investor protection funds, and other appropriate regulatory bodies.

15.2 Oversight Arrangements

Satisfactory information sharing and oversight agreements exist between the Ontario Securities Commission and the Foreign Regulator.

PART 16 IOSCO PRINCIPLES

16.1 IOSCO Principles

To the extent it is consistent with the laws of the foreign jurisdiction, the exchange adheres to the standards of the International Organization of Securities Commissions (**IOSCO**) including those set out in the "Principles for the Regulation and Supervision of Commodity Derivative Markets" (2011).

APPENDIX B

IN THE MATTER OF
THE SECURITIES ACT,
R.S.O. 1990, CHAPTER S. 5, AS AMENDED
(THE OSA)

AND

IN THE MATTER OF
THE COMMODITY FUTURES ACT,
R.S.O. 1990, CHAPTER C.20, AS AMENDED
(THE CFA)

AND

IN THE MATTER OF
THE LONDON METAL EXCHANGE

ORDER

(Section 147 of the OSA and sections 38 and 80 of the CFA)

WHEREAS London Metal Exchange (**LME**) has filed an application (**Application**) with the Ontario Securities Commission (**OSC**) requesting:

- (a) an order under Section 147 of the OSA exempting the LME from the requirement to be recognized as an exchange under Section 21(1) of the OSA (the **OSA Relief**);
- (b) an order under Section 80 of the CFA exempting the LME from the requirement to be registered as a commodity futures exchange under Section 15(1) of the CFA (the **Section 15 Relief**);
- (c) an order under Section 38 of the CFA exempting trades in contracts on the LME by a “hedger”, as defined in subsection 1(1) of the CFA (Hedger), from the registration requirements under Section 22 of the CFA (**Hedger Relief**); and
- (d) an order under Section 38 of the CFA exempting trades in contracts on the LME by a bank listed in Schedule I to the *Bank Act* (Canada) (**Bank**) entering orders as principal and for its own account only from the registration requirement under Section 22 of the CFA (**Bank Relief** and, together with the Hedger Relief, **Registration Relief**) (the OSA Relief, the Section 15 Relief and the Registration Relief, together the **Requested Relief**).

AND WHEREAS OSC Rule 91-503 *Trades in Commodity Futures Contracts and Commodity Futures Options Entered into on Commodity Futures Exchanges Situate Outside of Ontario* exempts trades of commodity futures contracts or commodity futures options made on commodity futures exchanges not registered with or recognized by the OSC under the CFA from sections 25 and 53 of the OSA;

AND WHEREAS the deemed rule titled *In the Matter of Trading in Commodity Futures Contracts and Commodity Futures Options Entered into on Commodity Futures Exchanges Situate Outside Canada Other Than Commodity Futures Exchanges in the United States of America* provides that section 33 of the CFA does not apply to trades in certain contracts made on the LME;

AND WHEREAS LME has represented to the OSC that:

1. The LME is a private company registered in England and Wales (registered number 2128666) whose registered office is at 10 Finsbury Square, London, EC2A 1AJ, United Kingdom (**UK**). The LME has no subsidiaries;
2. The LME is a wholly-owned subsidiary of LME Holdings Limited, a private limited company registered in England and Wales (registered number 4081218). LME Holdings Limited has no trading subsidiaries other than the LME;
3. LME Holdings Limited (the sole shareholder of the LME) in turn is a wholly owned subsidiary of HKEx Investment (UK) Limited, which is a wholly owned subsidiary of HKEx International Limited (a public limited company) registered in Hong Kong. HKEx International Limited is wholly owned by Hong Kong Exchanges and Clearing Limited, a publicly listed company registered in Hong Kong and listed on the Hong Kong stock exchange;

4. The LME receives a majority of its revenue from transaction fees for contracts executed through the LME;
5. The LME is subject to a comprehensive regulatory regime in the UK and Europe. As a UK Recognized Investment Exchange (**RIE**), the LME is subject to the UK *Financial Services and Markets Act 2000* (**FSMA**) and is regulated by the Financial Conduct Authority (**FCA**). The FCA fulfils its regulatory responsibilities within the framework established by FSMA and related legislation. As an RIE, the LME is also exempt from the general prohibition in respect of any “regulated activity” which is carried on as part of the LME’s business as an investment exchange;
6. The LME operates futures and options markets in thirteen industrial, base metals: (1) copper, (2) tin, (3) lead, (4) zinc, (5) primary aluminium, (6) nickel, (7) aluminium alloy, (8) NASAAC, steel billet, (9) cobalt, (10) molybdenum, (11) cash settled steel scrap, (12) cash settled steel rebar, and (13) regional aluminium. LME also offers London precious metal contracts in gold and silver futures (LMEprecious). The majority of all global non-ferrous trading business is conducted on the LME and the prices discovered on the LME’s trading platforms are used as global reference prices;
7. The LME may be described as an on-exchange forwards market. LME contracts (i.e. contracts under which metal is traded in accordance with the LME rules and regulations (**LME Rules**)) are based on physical settlement by the transfer of ownership of metal stored in listed warehouses; this guarantees price convergence as the far futures settlement dates converge on the cash settlement date (i.e. two days forward);
8. London Metal Exchange members (**Members**) who have specific permission from LME may trade LME contracts. All LME contracts are entered into on a principal to principal basis. LME contracts have at least one party being a Member of LME. LME participants who enter into LME contracts therefore deal off their own book, entering into an equivalent contract with customers for whom they are acting. In addition, organizations or an individual admitted to membership of the LME in accordance with the LME Rules will typically have entered into a separate contractual arrangement with their customers setting out the basis on which trades will be executed on the instructions of customers;
9. LME Clear Limited (**LME Clear**) has been established to act as the central counterparty in relation to all classes of contracts that are traded on the LME. LME Clear was incorporated on 21 April 2011 by LME as part of its global strategy to expand its clearing activities. LME Clear is also applying to the OSC for exemptive relief from recognition as a clearing agency under Section 21.2 of the OSA.
10. The LME does not have any offices or maintain other physical installations in Ontario or any other Canadian province or territory;
11. The LME proposes to offer prospective participants in Ontario access to the LMEselect system, the Inter-office Market and to Ring-dealing on the LME and to clearing support services. To obtain direct access to the LME, a prospective member in Ontario must execute a membership agreement in which the prospective member agrees to abide by the LME Rules and consent to submit to the jurisdiction of the Exchange. Prospective members in Ontario once admitted as members by LME (**Ontario Participants**) may access the Exchange. The LME Rules provide clear and transparent access criteria and requirements for all market participants, as well as minimum financial requirements for participants to maintain the financial integrity of the LME. The LME applies these criteria to all participants in an impartial manner;
12. LME is requesting the Hedger Relief and the Bank Relief in order for Ontario Participants (who are either Hedgers or Banks) to be able to access trading on the LME directly, without having to be registered as dealers under the CFA;
13. All contracts traded on the LME fall under the definitions of “commodity futures contract” or “commodity futures option” set out in section 1 of the CFA. The LME is therefore considered a “commodity futures exchange” as defined in section 1 of the CFA and is prohibited from carrying on business in Ontario unless it is registered or exempt from registration under section 15 of the CFA. The LME seeks to provide Ontario market participants with direct, electronic access to trading in LME contracts and may therefore be considered to be “carrying on business as a commodity futures exchange” in Ontario;
14. The LME is not registered with or recognized by the OSC as a commodity futures exchange under the CFA and no LME contracts have been accepted by the Director (as defined in the OSA) under the CFA. Therefore, LME contracts are considered “securities” under paragraph (p) of the definition of “security” set out in subsection 1(1) of the OSA and the LME is considered an “Exchange” under the OSA. Therefore, LME is prohibited from carrying on business in Ontario unless it is recognized or exempt from recognition under subsection 21(1) of the OSA. The LME seeks to provide Ontario market participants with direct, electronic access to trading in LME contracts and may therefore be considered to be “carrying on business as an Exchange” in Ontario;
15. The LME ensures that all applicants to become Members must satisfy certain criteria, including, among other things: validly organized and in good standing, good reputation, business integrity and adequate financial resources to assume the responsibilities and privileges of being a Member. Members are responsible for, among other things, compliance

with the LME Rules, as those rules relate to the entering and executing of transactions, and to comply with all applicable laws pertaining to the use of the LME;

AND WHEREAS the OSC will monitor developments in international and domestic capital markets and the LME's activities on an ongoing basis to determine whether it is appropriate for the OSC to continue to grant the Requested Relief and, if so, whether it is appropriate for the Requested Relief to continue to be granted subject to the terms and conditions set out in Schedule A to this order;

AND WHEREAS the LME has acknowledged to the OSC that the scope of the Requested Relief and the terms and conditions imposed by the OSC set out in Schedule A to this order may change as a result of its monitoring of developments in international and domestic capital markets or the LME's activities, or as a result of any changes to the laws in Ontario affecting trading in derivatives, commodity futures contracts, commodity futures options or securities;

AND WHEREAS based on the Application, together with the representations made by and acknowledgements of the LME to the OSC, the OSC has determined that:

- a. The LME satisfies the criteria for exemption set out in Appendix 1 of Schedule A; and
- b. The granting of the Requested Relief would not be prejudicial to the public interest.

IT IS HEREBY ORDERED by the OSC that:

- a. Pursuant to Section 147 of the OSA, the LME is exempt from the requirement to be recognized as an exchange under Section 21(1) of the OSA;
- b. Pursuant to Section 80 of the CFA, the LME is exempt from the requirement to be registered as a commodity futures exchange under Section 15(1) of the CFA;
- c. Pursuant to Section 38 of the CFA, trades in contracts on the LME by Hedgers who are Ontario Participants are exempt from the registration requirements under Section 22 of the CFA; and
- d. Pursuant to Section 38 of the CFA, trades in contracts on the LME by Banks who are Ontario Participants entering orders as principal and only for their own accounts are exempt from the registration requirements under Section 22 of the CFA.

PROVIDED THAT

- a. LME complies with the terms and conditions attached hereto as Schedule A; and
- b. The Bank Relief shall expire on the earliest of:
 - (i) The expiry of any transition period as may be provided by law, after the effective date of the repeal of the CFA;
 - (ii) Six months, or such other transition period as may be provided by law, after the coming into force of any amendment to Ontario commodity futures law (as defined in the CFA) or Ontario securities law (as defined in the OSA) that affects the dealer registration requirements in the CFA; and
 - (iii) Five years after the date of this order.

DATED _____, 2018.

SCHEDULE A

TERMS AND CONDITIONS

Meeting Criteria for Exemption

- 1 LME will continue to meet the criteria for exemption included in Appendix 1 to this Schedule A.

Regulation and Oversight of the LME

- 2 The LME will maintain its registration as a Recognised Investment Exchange (**RIE**) in accordance with the UK Financial Services and Markets Act (**FSMA**) and will continue to be subject to the regulatory oversight of the UK Financial Conduct Authority (**FCA**).
- 3 The LME will continue to comply with the ongoing requirements applicable to it as an RIE.
- 4 The LME must do everything within its control, which would include cooperating with the OSC as needed, to carry out its activities as an exchange exempted from recognition under subsection 21(1) of the OSA, as a commodity futures exchange exempted from registration under subsection 15(1) of the CFA, and in compliance with Ontario securities law and Ontario commodity futures law.

Access

- 5 LME will maintain and operate an electronic trading system where Members trade on a principal-to-principal basis. Members may also trade on the LME's inter-office market or in the LME's open-outcry dealing floor (the **Ring**).
- 6 The LME will not provide direct access to an Ontario Participant unless the Ontario Participant is appropriately registered to trade in LME contracts, is a Hedger or is a Bank; in making this determination, LME may reasonably rely on a written representation from the Ontario Participant that specifies that it is appropriately registered to trade in LME contracts or that it is a Hedger, or is a Bank and LME will notify such Ontario Participant that this representation is deemed to be repeated each time it enters an order for a LME contract.
- 7 Each Ontario Participant that intends to rely on the Hedger Relief will be required to, as part of its application or continued access to trading in LME contracts:
 - (a) represent that it is a Hedger;
 - (b) acknowledge that LME deems the Hedger representation to be repeated by the Ontario Participant each time it enters an order for a LME contract and that the Ontario Participant must be a Hedger for the purposes of each trade resulting from such an order;
 - (c) agree to notify LME if it ceases to be a Hedger;
 - (d) represent that it will only enter orders for its own account;
 - (e) acknowledge that it is a market participant under the CFA and is subject to applicable requirements; and
 - (f) acknowledge that its ability to continue to rely on the Hedger Relief in accessing trading on LME will be dependent on the OSC continuing to grant the relief and may be affected by changes to the terms and conditions imposed in connection with the Hedger Relief or by changes to Ontario securities laws or Ontario commodity futures laws pertaining to derivatives, commodity futures contracts, commodity futures options or securities.
- 8 Each Ontario Participant that intends to rely on the Bank Relief will be required to, as part of its application documentation or continued access to trading in LME contracts:
 - (a) represent that it will only enter orders as principal and for its account only;
 - (b) represent that it is a Bank (the **Canadian Bank Representation**);
 - (c) acknowledge that LME deems the Canadian Bank Representation to be repeated by the Ontario Participant each time it enters an order for a LME contract and that the Ontario Participant must be a Bank for the purposes of each trade resulting from such an order;

- (d) agree to notify LME if it ceases to be a Bank;
 - (e) acknowledge that the Bank Relief may be affected by changes to the terms and conditions imposed in connection with the Bank Relief or by changes to Ontario securities laws or Ontario commodity futures laws pertaining to derivatives, commodity futures contracts, commodity futures options or securities; and
 - (f) represent that it is not engaging in activities prohibited by its governing legislation.
- 9 The LME will require Ontario Participants to notify LME if their applicable registration has been revoked, suspended or amended by the OSC (if applicable) or if they have ceased to be a Bank and, following notice from the Ontario Participant or the OSC and subject to applicable laws, LME will promptly restrict the Ontario Participant's access to the LME if the Ontario Participant is no longer appropriately registered with the OSC or is no longer a Bank.
- 10 The LME must make available to Ontario Participants appropriate training for each person who has access to trade in LME contracts.

Trading by Ontario Participants

- 11 The LME will not provide access to an Ontario Participant to trading in exchange-traded products of an exchange other than those of the LME, unless such other exchange has sought and received appropriate regulatory standing in Ontario.
- 12 The LME will not provide access to an Ontario Participant to trading in LME contracts other than those that meet the definition of "commodity futures contract" or "commodity futures option" as defined in subsection 1(1) of the CFA, and which also fall under paragraph (p) of the definition of "security" in subsection 1(1) of the OSA, without prior OSC approval or pursuant to the Requested Relief.

Submission to Jurisdiction and Agent for Service

- 13 With respect to a proceeding brought by the OSC arising out of, related to, concerning or in any other manner connected with the OSC's regulation and oversight of the activities of the LME in Ontario, the LME will submit to the non-exclusive jurisdiction of (i) the courts and administrative tribunals of Ontario and (ii) an administrative proceeding in Ontario.
- 14 The LME will file with the OSC a valid and binding appointment of Norton Rose Fulbright Canada LLP as the agent for service in Ontario upon which the OSC may serve a notice, pleading, subpoena, summons or other process in any action, investigation or administrative, criminal, quasi-criminal, penal or other proceeding arising out of or relating to or concerning the OSC's regulation and oversight of the LME's activities in Ontario.

Disclosure

- 15 The LME will provide to its Ontario Participants disclosure that states that:
- (a) rights and remedies against the LME may only be governed by the laws of England and Wales, rather than the laws of Ontario, and may be required to be pursued in England and Wales rather than in Ontario;
 - (b) the rules applicable to trading on the LME may be governed by the laws of the UK, rather than the laws of Ontario; and
 - (c) The LME is regulated by the FCA, rather than the OSC.

Filings with the FCA

- 16 The LME will promptly provide staff of the OSC copies of all material rules of the LME, and material amendments to those rules, that it files with the FCA.
- 17 The LME will promptly provide staff of the OSC copies of all material contract specifications and material amended contract specifications that it files with the FCA.
- 18 The LME will promptly provide staff of the OSC the following information to the extent it is required to file such information with the FCA:

- (a) the annual Board of Directors' report regarding the activities of the Board and its committees;
- (b) the annual financial statements of the LME;
- (c) details of any material legal proceeding instituted against the LME;
- (d) notification that the LME has instituted a petition for a judgment of bankruptcy or insolvency or similar relief, or to wind up or liquidate the LME or has a proceeding for any such petition instituted against it; and
- (e) the appointment of a receiver or the making of any voluntary arrangement with creditors.

Prompt Notice or Filing

- 19 The LME will promptly notify staff of the OSC of any of the following:
- (a) any material change to its business or operations or the information provided in the Application, including, but not limited to:
 - (i) changes to the regulatory oversight by the FCA;
 - (ii) the corporate governance structure of the LME;
 - (iii) the access model, including eligibility criteria, for Ontario Participants;
 - (iv) systems and technology; and
 - (v) the clearing and settlement arrangements for the LME;
 - (b) any change in the LME's regulations or the laws, rules and regulations in the UK relevant to futures and options where such change may materially affect its ability to meet the criteria set out in Appendix 1 to this schedule;
 - (c) any condition or change in circumstances whereby the LME is unable or anticipates it will not be able to continue to meet its obligations under any applicable requirements of the FCA or the FSMA regulations;
 - (d) any revocation or suspension of, or amendment to, the LME's registration as an RIE by the FCA or if the basis on which the LME's registration as a RIE was granted has significantly changed;
 - (e) any known investigations of, or disciplinary action against, the LME by the FCA or any other regulatory authority to which it is subject;
 - (f) any matter known to the LME that may affect its financial or operational viability, including, but not limited to, any significant system failure or interruption; and
 - (g) any default, insolvency, or bankruptcy of any Member known to the LME or its representatives that may have a material, adverse impact upon the LME or any Ontario Participant.
- 20 LME will promptly file with staff of the OSC copies of any enforcement reports regarding LME once issued as final by the FCA.

Quarterly Reporting

- 21 LME will maintain the following updated information and submit such information in a manner and form acceptable to the OSC on a quarterly basis (within 30 days of the end of each calendar quarter), and at any time promptly upon the request of staff of the OSC:
- (a) a current list of all Ontario Participants, specifically identifying for each Ontario Participant:
 - (i) its status as LME or LME Clear Members , and
 - (ii) the basis upon which it represented to the LME that it could be provided with direct access (i.e. that it is appropriately registered to trade in the LME contracts or benefits from another form of exemption);

- (b) a list of all Ontario Participants against whom disciplinary action has been taken in the last quarter by the LME or, to the best of LME's knowledge, by any non-Canadian regulatory bodies with respect to such Ontario Participants' activities on the LME;
- (c) a list of all referrals to the LME Head of Risk, Regulation and Compliance by the LME surveillance team concerning Ontario Participants;
- (d) a list of all Ontario applicants for status as an Ontario Participant who were denied such status or access to the LME during the quarter;
- (e) a list of all new by-laws, rules, and contract specifications, and changes to by-laws, rules and contract specifications, not already reported;
- (f) a list of all LME contracts available for trading during the quarter, identifying any additions, deletions or changes since the prior quarter;
- (g) for each LME contract,
 - (i) the total trading volume and value originating from Ontario Participants, presented on a per Ontario Participant basis, and
 - (ii) the proportion of worldwide trading volume and value on the LME conducted by Ontario Participants, presented in the aggregate for such Ontario Participants; and
- (h) a list outlining each incident of a significant system outage that occurred at any time during the quarter for any system impacting Ontario Participants' trading activity, including trading, routing or data, specifically identifying the date, duration and reason for the outage, and noting any corrective action taken.

Annual Reporting

- 22 LME will arrange to have the annual audited financial statements of the LME filed with the OSC promptly after their issuance.

Reporting

- 23 If an IT Service Auditor's Report (**Report**) is prepared for the LME, the LME will promptly file with the OSC the Report after the Report is issued as final by its independent auditor.

Information Sharing

- 24 The LME will provide information (including additional periodic reporting) as may be requested from time to time by, and otherwise cooperate with, the OSC or its staff, subject to any applicable privacy or other laws (including solicitor-client privilege) governing the sharing of information and the protection of personal information.

APPENDIX 1

CRITERIA FOR EXEMPTION

PART 1 REGULATION OF THE EXCHANGE

1.1 Regulation of the Exchange

The exchange is regulated in an appropriate manner in another jurisdiction by a foreign regulator (**Foreign Regulator**).

1.2 Authority of the Foreign Regulator

The Foreign Regulator has the appropriate authority and procedures for oversight of the exchange. This includes regular, periodic oversight reviews of the exchange by the Foreign Regulator.

PART 2 GOVERNANCE

2.1 Governance

The governance structure and governance arrangements of the exchange ensure:

- (a) effective oversight of the exchange,
- (b) that business and regulatory decisions are in keeping with its public interest mandate,
- (c) fair, meaningful and diverse representation on the board of directors (Board) and any committees of the Board, including:
 - (i) appropriate representation of independent directors, and
 - (ii) a proper balance among the interests of the different persons or companies using the services and facilities of the exchange,
- (d) the exchange has policies and procedures to appropriately identify and manage conflicts of interest, and
- (e) there are appropriate qualifications, remuneration, limitation of liability and indemnity provisions for directors, officers and employees of the exchange.

2.2 Fitness

The exchange has policies and procedures under which it will take reasonable steps, and has taken such reasonable steps, to ensure that each director and officer is a fit and proper person.

PART 3 REGULATION OF PRODUCTS

3.1 Review and Approval of Products

The products traded on the exchange and any changes thereto are reviewed by the Foreign Regulator, and are either approved by the Foreign Regulator or are subject to requirements established by the Foreign Regulator that must be met before implementation of a product or changes to a product.

3.2 Product Specifications

The terms and conditions of trading the products are in conformity with the usual commercial customs and practices for the trading of such products.

3.3 Risks Associated with Trading Products

The exchange maintains adequate provisions to measure, manage and mitigate the risks associated with trading products on the exchange including, but not limited to, margin requirements, intra-day margin calls, daily trading limits, price limits, position limits, and internal controls.

PART 4 ACCESS

4.1 Fair Access

- (a) The exchange has established appropriate written standards for access to its services including requirements to ensure
 - (i) participants are appropriately registered as applicable under Ontario securities laws or Ontario commodity futures laws, or exempted from these requirements,
 - (ii) the competence, integrity and authority of systems users, and
 - (iii) systems users are adequately supervised.
- (b) The access standards and the process for obtaining, limiting and denying access are fair, transparent and applied reasonably.
- (c) The exchange does not unreasonably prohibit, condition or limit access by a person or company to services offered by it.
- (d) The exchange does not
 - (i) permit unreasonable discrimination among participants, or
 - (ii) impose any burden on competition that is not reasonably necessary and appropriate.

PART 5 REGULATION OF PARTICIPANTS ON THE EXCHANGE

5.1 Regulation

The exchange has the authority, resources, capabilities, systems and processes to allow it to perform its regulation functions, whether directly or indirectly through a regulation services provider, including setting requirements governing the conduct of its participants, monitoring their conduct, and appropriately disciplining them for violations of exchange requirements.

PART 6 RULEMAKING

6.1 Purpose of Rules

- (a) The exchange has rules, policies and other similar instruments (Rules) that are designed to appropriately govern the operations and activities of participants.
- (b) The Rules are not contrary to the public interest and are designed to
 - (i) ensure compliance with applicable legislation,
 - (ii) prevent fraudulent and manipulative acts and practices,
 - (iii) promote just and equitable principles of trade,
 - (iv) foster co-operation and co-ordination with persons or companies engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in the products traded on the exchange,
 - (v) provide a framework for disciplinary and enforcement actions, and
 - (vi) ensure a fair and orderly market.

PART 7 DUE PROCESS

7.1 Due Process

For any decision made by the exchange that affects a participant, or an applicant to be a participant, including a decision in relation to access, exemptions, or discipline, the exchange ensures that:

- (a) parties are given an opportunity to be heard or make representations, and
- (b) it keeps a record of, gives reasons for, and provides for appeals or reviews of its decisions.

PART 8 CLEARING AND SETTLEMENT

8.1 Clearing Arrangements

The exchange has appropriate arrangements for the clearing and settlement of transactions through a clearing house.

8.2 Regulation of the Clearing House

The clearing house is subject to acceptable regulation.

8.3 Authority of Regulator

A foreign regulator has the appropriate authority and procedures for oversight of the clearing house. This includes regular, periodic regulatory examinations of the clearing house by the foreign regulator.

8.4 Access to the Clearing House

- (a) The clearing house has established appropriate written standards for access to its services.
- (b) The access standards for clearing members and the process for obtaining, limiting and denying access are fair, transparent and applied reasonably.

8.5 Sophistication of Technology of Clearing House

The exchange has assured itself that the information technology used by the clearing house has been adequately reviewed and tested and provides at least the same level of safeguards as required of the exchange.

8.6 Risk Management of Clearing House

The exchange has assured itself that the clearing house has established appropriate risk management policies and procedures, contingency plans, default procedures and internal controls.

PART 9 SYSTEMS AND TECHNOLOGY

9.1 Systems and Technology

Each of the exchange's critical systems has appropriate internal controls to ensure completeness, accuracy, integrity and security of information, and, in addition, has sufficient capacity and business continuity plans to enable the exchange to properly carry on its business. Critical systems are those that support the following functions:

- (a) order entry,
- (b) order routing,
- (c) execution,
- (d) trade reporting,
- (e) trade comparison,
- (f) data feeds,
- (g) market surveillance,
- (h) trade clearing, and
- (i) financial reporting.

9.2 Information Technology Risk Management Procedures

The exchange has appropriate risk management procedures in place including those that handle trading errors, trading halts and circuit breakers.

PART 10 FINANCIAL VIABILITY

10.1 Financial Viability

The exchange has sufficient financial resources for the proper performance of its functions and to meet its responsibilities.

PART 11 TRANSPARENCY

11.1 Transparency

The exchange has adequate arrangements to record and publish accurate and timely trade and order information. This information is provided to all participants on an equitable basis.

PART 12 RECORD KEEPING

12.1 Record Keeping

The exchange has and maintains adequate systems in place for the keeping of books and records, including, but not limited to, those concerning the operations of the exchange, audit trail information on all trades, and compliance with, and/or violations of exchange requirements.

PART 13 OUTSOURCING

13.1 Outsourcing

Where the exchange has outsourced any of its key services or systems to a service provider, it has appropriate and formal arrangements and processes in place that permit it to meet its obligations and that are in accordance with industry best practices.

PART 14 FEES

14.1 Fees

- (a) All fees imposed by the exchange are reasonable and equitably allocated and do not have the effect of creating an unreasonable condition or limit on access by participants to the services offered by the exchange.
- (b) The process for setting fees is fair and appropriate, and the fee model is transparent.

PART 15 INFORMATION SHARING AND OVERSIGHT ARRANGEMENTS

15.1 Information Sharing and Regulatory Cooperation

The exchange has mechanisms in place to enable it to share information and otherwise co-operate with the OSC, self-regulatory organizations, other exchanges, clearing agencies, investor protection funds, and other appropriate regulatory bodies.

15.2 Oversight Arrangements

Satisfactory information sharing and oversight agreements exist between the OSC and the Foreign Regulator.

PART 16 IOSCO PRINCIPLES

16.1 IOSCO Principles

To the extent it is consistent with the laws of the foreign jurisdiction, the exchange adheres to the standards of the International Organisation of Securities Commissions including those set out in the "Principles for the Regulation and Supervision of Commodity Derivative Markets" (2011).