

ALBERTA SECURITIES COMMISSION

INTERIM RECOGNITION ORDER:  
DERIVATIVES EXCHANGE

Citation: Re Net Energy Inc., 2019 ABASC 134

Date: 20190829

Net Energy Inc.

**Background**

1. On February 1, 2016, the Alberta Securities Commission (the **Commission**) issued an order (the **2016 Order**, cited as *Re Net Energy Inc.*, 2016 ABASC 25) recognizing Net Energy Inc. (**Net Energy**) as an exchange under section 62 of the *Securities Act* (Alberta) (the **Act**) and granting associated relief.
2. On February 1, 2019, the Commission issued an order (the **First Variation Order**, cited as *Re Net Energy Inc.*, 2019 ABASC 21) extending the expiry date of the 2016 Order to July 2, 2019.
3. On July 2, 2019, the Commission issued an order (the **Second Variation Order**, cited as *Re Net Energy Inc.*, 2019 ABASC 105) extending the expiry date of the 2016 Order to August 30, 2019 (collectively, the 2016 Order, the First Variation Order and the Second Variation Order are referred to as the **Current Order**).
4. On January 23, 2019, Net Energy applied to the Commission pursuant to section 62 of the Act for a new order which would, among other things:
  - (a) continue its recognition as a derivatives exchange;
  - (b) reflect the movement of the Voice Brokers (as defined below) employed by Net Energy into a separate division and the associated registration of Net Energy and the Voice Brokers as restricted dealers pursuant to the Act;
  - (c) reflect the negotiation of a clearing agreement with the Chicago Mercantile Exchange Inc. (the **CME**) or with another clearing agency recognized or exempted from recognition under section 67 of the Act; and
  - (d) continue the following relief granted under the Current Order:
    - (i) under section 144(1) of the Act, an exemption from the registration requirement in section 75(1) of the Act for Contract Participants (as defined below) (the **Registration Relief**); and
    - (ii) under section 15.1(1) of National Instrument 21-101 *Marketplace Operation* (**NI 21-101**), an exemption from the requirements of NI 21-101.

5. The Voice Brokers have been moved into a separate division and, on July 9, 2019, Net Energy and its Voice Brokers were registered as restricted dealers pursuant to the Act.

### Interpretation

6. Terms defined in the Act or National Instrument 14-101 *Definitions* have the same meaning in this order unless otherwise defined herein.

### Representations

7. Net Energy represents as follows:
- (a) Net Energy is a corporation incorporated under the laws of the Province of Alberta and is based in Calgary, Alberta;
  - (b) Net Energy offers contracts based upon energy based indices compiled, maintained and published by Net Energy (**Contracts**);
  - (c) Net Energy makes the Contracts available for trading on an electronic trading platform owned, operated, leased, licensed or otherwise made available by Net Energy (the **Exchange Trading Platform**);
  - (d) trades in Contracts on the Exchange Trading Platform may only be executed as follows:
    - (i) directly, as principal, by contract participants that have entered into a standard-form user agreement with Net Energy establishing minimum qualification standards (**Minimum Qualification Standards**) for such exchange participants (**Customer User Agreement**) (each, a **Contract Participant**); or
    - (ii) indirectly by Contract Participants through voice brokers that meet the qualification standards set by Net Energy (**Voice Broker Standards**) (each, a **Voice Broker**) (together, Contract Participants and Voice Brokers are referred to as **Exchange Participants**);
  - (e) trades in Contracts on the Exchange Trading Platform are made by Exchange Participants in accordance with the Customer User Agreement, the rules applicable to the Exchange Trading Platform, and related regulations, specifications and policies established, monitored and enforced by Net Energy (collectively, the **Rules**);
  - (f) all trades in Contracts are executed on the Exchange Trading Platform during hours prescribed by Net Energy for trading in Contracts;
  - (g) the Exchange Trading Platform provides a competitive, open and efficient market and mechanism for executing trades in Contracts that protects the price discovery process, including pre-trade transparency, of trading on the Exchange Trading Platform; and

- (h) Net Energy complies, to the extent such principles are not inconsistent with Alberta securities laws, with *Principles for Oil Price Reporting Agencies*, as amended from time to time, developed by the Board of the International Organization of Securities Commissions.

### **Undertakings**

8. Net Energy undertakes:

- (a) not to enter any contract, agreement or arrangement that may limit its ability to comply with Alberta securities laws;
- (b) to operate the Exchange Trading Platform in accordance with the operating requirements set out in Appendix A to this order (the **Operating Requirements**);
- (c) to report to the Commission in accordance with the reporting requirements set out in Appendix B to this order (the **Reporting Requirements**);
- (d) to employ reasonable procedures for monitoring and enforcing compliance with these undertakings (the **Undertakings**), the Operating Requirements and the Reporting Requirements;
- (e) to take all reasonable steps to ensure that its operations do not interfere with fair and orderly markets;
- (f) to establish, monitor and enforce compliance with the Rules which must include provisions that are designed to: (i) govern the terms and conditions of the Contracts, the operation of the Exchange Trading Platform, access to the Exchange Trading Platform, and the conduct of the Exchange Participants; (ii) ensure compliance with securities legislation; (iii) prevent fraudulent, manipulative and abusive acts and practices on the Exchange Trading Platform; (iv) promote fair, orderly, just and equitable trading on the Exchange Trading Platform; (v) foster cooperation and coordination with persons or companies engaged in regulating, clearing, settling, and processing information relating to trading on the Exchange Trading Platform; and (vi) provide appropriate sanctions for violations of the Rules;
- (g) to investigate any possible violation of the Rules promptly, either as a result of Net Energy's obligations under paragraph (f) or upon request from the Executive Director of the Commission;
- (h) to ensure the accuracy and completeness of any communication with the Commission and any information made available to Exchange Participants or to the public, including ensuring that no material information is omitted;
- (i) to comply with any request from the Executive Director of the Commission relating to the oversight of Net Energy as an exchange;
- (j) during the term of this order, to pursue the following:

- (i) a direct clearing agreement with a clearing agency recognized or exempted from recognition under section 67 of the Act; and
  - (ii) listing of its own proprietary contracts on the Exchange Trading Platform;
- and
- (k) to notify the Commission immediately upon Net Energy becoming aware that any of the representations in this order are no longer true and accurate or that it has become unable to comply with any of the Undertakings.

**Decision**

Based on the above representations and Undertakings, the Commission, being satisfied that it would not be prejudicial to the public interest to do so:

- (a) under
  - (i) section 62 of the Act, continues to recognize Net Energy as a derivatives exchange on an interim basis,
  - (ii) section 144(1) of the Act, grants the Registration Relief, and
  - (iii) section 15.1(1) of NI 21-101, exempts Net Energy from the requirements of NI 21-101,provided that, and for so long as, Net Energy continues to comply with the Undertakings; and
- (b) under section 214(1) of the Act, revokes the Current Order.

This order expires on August 30, 2021.

**For the Commission:**

*"original signed by"*

Tom Cotter  
Vice-Chair

*"original signed by"*

Kari Horn  
Vice-Chair

## APPENDIX A Operating Requirements

This Appendix forms a part of, and adopts terms defined in, the order governing Net Energy's interim recognition as a derivatives exchange (the **Order**).

### *Access Requirements*

1. Rules concerning access to the Exchange Trading Platform must not unreasonably prohibit, condition or limit access by a person or company to the Exchange Trading Platform or permit unreasonable discrimination among Exchange Participants.
2. Access to the Exchange Trading Platform is restricted to Exchange Participants and Net Energy will take reasonable steps to prevent third parties, including Exchange Participants, from providing unauthorized access.
3. Net Energy must take reasonable steps to ensure that each officer and director, or other individual performing a similar function or occupying a similar position, of each entity applying to become an Exchange Participant, is a fit and proper person for that role. When conducting this assessment, Net Energy must consider whether the past conduct of such individual affords reasonable grounds for the belief that the individual will perform the individual's duties with integrity.
4. If Net Energy makes a decision denying or suspending access of an Exchange Participant to the Exchange Trading Platform or denying an application to be an Exchange Participant, Net Energy must ensure that the party being denied or suspended has been given an opportunity to be heard and the party is able to appeal the decision or otherwise have it reviewed.
5. Net Energy must not impose any restriction on competition among Exchange Participants that is not reasonably necessary or appropriate.

### *Fees*

6. Net Energy's process for setting fees must be fair and appropriate, and the fee model must be readily accessible to Exchange Participants and applicants to become Exchange Participants. All fees imposed by Net Energy must be equitably assessed and consistent with the requirements for access to the Exchange Trading Platform.

### *Financial Integrity of Transactions*

7. Net Energy must take steps to ensure the financial integrity of transactions, including the following:
  - (a) requiring trades in Contracts executed on the Exchange Trading Platform to be cleared through a clearing agency recognized or exempted from recognition under section 67 of the Act (the **Clearing Agency**) and which Clearing Agency clears, settles and guarantees to its members (**Clearing Members**) the performance of all trades in Contracts executed on the Exchange Trading Platform;

- (b) requiring Exchange Participants either to be Clearing Members or to use a Clearing Member to clear trades in Contracts executed on the Exchange Trading Platform;
- (c) ensuring the Rules authorize Net Energy to exercise emergency authority, including the authority to: (a) co-operate with the Clearing Agency or any Clearing Member pursuant to any liquidation or transfer of open positions of an Exchange Participant carried out by that Clearing Agency or Clearing Member; and (b) suspend or curtail trading in Contracts;
- (d) confirming, on a periodic basis and as otherwise required, that each Contract Participant continues to meet the Minimum Qualification Standards; and
- (e) confirming, on a periodic basis and as otherwise required, that each Voice Broker continues to meet the Voice Broker Standards.

***Market Surveillance and Market Integrity***

8. Net Energy must have effective automated or manual programs for monitoring trading activity on the Exchange Trading Platform to identify:
  - (a) in real time, disorderly trading and any market or system anomalies; and
  - (b) within 24 hours after the completion of the trading day, indications of fraud, manipulation or other market abuses

(the **Surveillance System**).
9. Net Energy must ensure that Contracts traded on the Exchange Trading Platform are not readily susceptible to manipulation.
10. Net Energy must establish risk-control mechanisms, including powers to:
  - (a) address trading errors and system malfunctions (including the power to cancel or otherwise modify trades); and
  - (b) impose trading halts or suspensions where market conditions prescribed by Net Energy occur.
11. Trade price adjustments and trade cancellations must be visible on the Exchange Trading Platform to the Exchange Participants.
12. Net Energy must regularly monitor, for a Contract:
  - (a) the availability and pricing of the commodity making up the index with reference to which such Contract will be settled; and
  - (b) the continued appropriateness of the methodology for deriving such index.

13. Net Energy must promptly amend any index methodologies that result, or are likely to result, in manipulation, price distortions or market disruptions, or it must impose new methodologies to resolve the threat of manipulation, price distortions or market disruptions.
14. If a Contract is settled by reference to the price of a contract or commodity traded on another derivatives exchange or venue, including a price or index derived from prices on another derivatives exchange or venue, Net Energy must require Exchange Participants to provide Net Energy with their positions in the reference markets as the Contract approaches settlement, unless Net Energy has entered into an information sharing agreement with the other derivatives exchange or venue for the purpose of obtaining such information directly from the other derivatives exchange or venue.

### ***Recordkeeping***

15. Net Energy must maintain for a period of 7 years, in a form and manner acceptable to the Commission, and make available to the Commission upon request, records of all activities relating to Net Energy carrying on business as a derivatives exchange. Without limiting the foregoing, Net Energy must keep records of:
  - (a) each decision to grant, deny or limit access to the Exchange Trading Platform, and the reasons therefor;
  - (b) any other decisions made by Net Energy that significantly affect an Exchange Participant, or an applicant to be an Exchange Participant, and the reasons therefor; and
  - (c) all trading activities on the Exchange Trading Platform.
16. The records required under paragraph 15(c) (the **Audit Trail**) must be sufficient to facilitate, within a reasonable period of time, the accurate reconstruction of all trades in Contracts, and must consist of:
  - (a) an unalterable, sequentially identified original source document for each order and each modification or cancellation of an order or trade containing
    - (i) the terms of each order and each modification or cancellation of an order or trade,
    - (ii) an Exchange Participant account identifier, and
    - (iii) the time and date of order entry and modification or cancellation of an order or trade;and
  - (b) an electronic transaction history database, with electronic surveillance and analysis capability, that includes

- (i) a history of all orders and trades and of modifications and cancellations of orders and trades,
- (ii) all data entered into the order entry or matching system for the transaction to match and clear,
- (iii) identification of each account to which Contracts are allocated, and
- (iv) timing and sequencing data.

17. The Rules must establish the terms upon which Exchange Participants are required to keep records of their trading activities on the Exchange Trading Platform, including records of their activity in any underlying commodity and related derivatives markets.

***Regulation of Exchange Participants***

18. Net Energy must maintain and enforce procedures that empower it to:

- (a) investigate potential violations of the Rules;
- (b) make determinations as to whether violations have occurred;
- (c) impose appropriate sanctions for such violations; and
- (d) provide a mechanism and facilities for the resolution of disputes among Exchange Participants.

19. The Rules must provide that Net Energy may make enquiries or conduct investigations relating to the activities of Exchange Participants to ensure compliance with or enforcement of the Rules and, in relation to any such enquiries or investigations, the Rules must give Net Energy access to an Exchange Participant's records of trading activity upon reasonable notice to the Exchange Participant.

***Availability of Information***

20. Net Energy must make available to the Commission, Exchange Participants and the public, accurate, complete and current information concerning:

- (a) the terms and conditions of Contracts;
- (b) the Rules and mechanisms for executing transactions on the Exchange Trading Platform; and
- (c) the Rules describing the operation of the Exchange Trading Platform.

21. Net Energy must publish:

- (a) all changes to the Rules on the date of implementation of the changes; and
- (b) details of a new or amended Contract on the date of listing of the Contract.



22. Net Energy must report to the public directly, or indirectly through an information vendor, daily information on settlement prices, volume, open interest, and opening and closing ranges for actively traded Contracts by the close of the next business day following the day to which the information pertains.

### ***Conflicts of Interest***

23. Net Energy must establish, monitor and enforce compliance with policies and procedures that identify and manage any conflicts of interest arising from the operation of its exchange or the services it provides.

### ***Governance***

24. Net Energy's governance arrangements must be designed to ensure effective oversight of the Exchange Trading Platform.
25. Net Energy must take reasonable steps to ensure that each officer and director, or other individual performing a similar function or occupying a similar position, of Net Energy, is a fit and proper person for that role. When conducting this assessment, Net Energy must consider whether the past conduct of such individual affords reasonable grounds for the belief that the individual will perform the individual's duties with integrity.

### ***System Safeguards***

26. Net Energy must maintain a program of risk analysis and oversight designed to identify, manage and minimize sources of operational risk, through the development of appropriate controls and procedures, and the development of automated systems that are reliable, secure and have adequate scalable capacity (an **Enterprise Risk Management Program**).
27. Net Energy must have a business continuity and disaster recovery plan designed to ensure that trading can resume on the Exchange Trading Platform after trading is disrupted. Under normal commercial circumstances, Net Energy should ensure capability to resume trading by the next business day following the disruption.
28. Net Energy must conduct regular objective testing and review of its automated systems and business continuity and disaster recovery plan and retain records of such tests and reviews for a period of 7 years.
29. Where necessary and to the extent practicable, Net Energy will coordinate and test its business continuity and disaster recovery plan with those of its essential service providers and Exchange Participants upon whom Net Energy depends to provide liquidity.

### ***Resources and Outsourcing***

30. Net Energy must have access to sufficient financial, operational, managerial and regulatory compliance and oversight resources to carry out its functions and regulatory responsibilities.
31. Net Energy must ensure that any arrangements for outsourcing of services will not impair its ability to satisfy its obligations under the Order.

## **APPENDIX B**

### **Reporting Requirements**

This Appendix forms a part of, and adopts terms defined in, the order governing Net Energy's interim recognition as a derivatives exchange (the **Order**).

#### ***Event Reporting***

1. Net Energy will notify the Commission as soon as reasonably practicable, and in any event not later than 10 business days prior to:
  - (a) any significant change to Net Energy's constating documents or bylaws;
  - (b) any significant change to the Minimum Qualification Standards;
  - (c) any significant change to the Voice Broker Standards;
  - (d) any significant change to the Rules or any new Rules;
  - (e) entering into an agreement to outsource key Exchange Trading Platform functions;
  - (f) any significant change in the design or operation of the Exchange Trading Platform;
  - (g) any change in the beneficial ownership of Net Energy;
  - (h) any significant change to Net Energy's automated systems that may affect the reliability, security or adequate scalable capacity of such systems;
  - (i) any significant changes to the Surveillance System;
  - (j) any significant changes to the Enterprise Risk Management Program;
  - (k) engaging in a new type of business activity or ceasing to engage in a business activity in which Net Energy is then engaged;
  - (l) any significant change to the fees charged by Net Energy, including the addition of new fees; or
  - (m) each significant change to an existing agreement or any new agreement between Net Energy and any third party.
2. Prior to implementing a change contemplated in paragraph 1(a), 1(d) or 1(l), Net Energy will file with the Commission, concurrently with the notification required under such paragraph, a certification by Net Energy that the change does not conflict with the terms of the Order.
3. Net Energy will not implement a change contemplated in paragraph 1(b) or 1(c) without the prior written approval of the Executive Director of the Commission.

4. Net Energy will promptly notify the Commission upon becoming aware of:
  - (a) any electronic trading halts or systems malfunctions that occur for 15 minutes or more;
  - (b) cyber-security incidents or targeted threats that jeopardize automated system operation, reliability, security or capacity;
  - (c) any event triggering the activation of Net Energy's business continuity and disaster recovery plan;
  - (d) any change to Net Energy's board membership or senior management team or any significant change to Net Energy's corporate governance or corporate structure, unless a notification of the change has been made under paragraph 1(a);
  - (e) any monetary default, insolvency or bankruptcy or similar proceeding of Net Energy, any of its subsidiaries or affiliates, any of the directors or officers of Net Energy or its subsidiaries or affiliates that may have a material adverse effect on the financial or operational viability of Net Energy or the Exchange Trading Platform, including the particulars of the default, insolvency or bankruptcy and the resolution proposed. Net Energy must also provide the Commission with information regarding the impact of the default on the adequacy of Net Energy's financial resources;
  - (f) any order, sanction or other directive received from, or imposed by, a regulatory or government body against Net Energy, any of its subsidiaries or affiliates, or any of the directors or officers of Net Energy or its subsidiaries or affiliates;
  - (g) any investigations by a regulatory or government body against Net Energy, any of its subsidiaries or affiliates, or any of the directors or officers of Net Energy or its subsidiaries or affiliates;
  - (h) any criminal or quasi-criminal charges brought against Net Energy, any of its subsidiaries or affiliates, or any of the directors or officers of Net Energy or its subsidiaries or affiliates; or
  - (i) any civil suits brought against Net Energy, any of its subsidiaries or affiliates, or any of the directors or officers of Net Energy or its subsidiaries or affiliates, that would likely have a significant impact on Net Energy's business.
5. Net Energy will notify the Commission as soon as possible, and in any event no later than 2 business days from the date of occurrence, of each new or amended pricing methodology for indices upon which any Contracts are based.
6. In the event that an Exchange Participant defaults under an agreement with Net Energy and such default is not resolved within 2 business days, Net Energy will promptly notify the Commission of the particulars of the default, the parties involved in the default, and the method of resolution proposed.

***Contracts***

7. Not later than one business day prior to Net Energy listing a new or amended Contract for trading on the Exchange Trading Platform, Net Energy will file with the Commission a certification by Net Energy that the new or amended Contract complies with the terms of the Order.

***Quarterly Reporting***

8. Net Energy will provide to the Commission, within 60 days of the end of each quarter of the financial year:
  - (a) a list of current Exchange Participants;
  - (b) interim financial statements prepared in the same manner as the annual financial statements, but not audited;
  - (c) any non-significant changes to the Rules;
  - (d) a reasonable calculation of Net Energy's projected operating costs over a 12-month period to determine if Net Energy's financial resources are sufficient. Financial resources available to satisfy the requirements of this paragraph (d) may include Net Energy's own capital, and any other financial resource deemed acceptable by the Commission. However, financial resources allocated by Net Energy to meet the requirements of this paragraph (d) must include unencumbered, liquid financial assets (i.e., cash highly liquid securities, or both) equal to at least 6 months' operating costs. If any portion of such financial resources is not sufficiently liquid, Net Energy may take into account a committed line of credit or similar facility for the purpose of meeting this requirement. Net Energy shall have reasonable discretion in determining the methodology used to compute such projected operating costs;
  - (e) the current market value of each financial resource used to meet Net Energy's projected operating costs under paragraph (d). Reductions in value to reflect market and credit risk must be applied as appropriate;
  - (f) sufficient documentation to explain the methodology used to compute Net Energy's projected operating costs under paragraph (d);
  - (g) sufficient documentation to explain the basis for Net Energy's determinations regarding the valuation and liquidity of its financial resources under paragraphs (d) and (e); and
  - (h) copies of any agreements establishing or amending a credit facility, insurance coverage, or other arrangement evidencing or otherwise supporting Net Energy's conclusions regarding its projected operating costs.

**Annual Reporting**

9. Net Energy will provide to the Commission within 90 days of the end of each financial year:
- (a) annual financial statements that include a statement of comprehensive income, a statement of changes in equity, and a statement of cash flows for the most recently completed financial year with comparatives for the financial year immediately preceding the most recently completed financial year; a statement of financial position as at the end of the most recently completed financial year and the financial year immediately preceding the most recently completed financial year, and notes to the financial statements. Such annual financial statements must be prepared in accordance with IFRS, disclose an unreserved statement of compliance with Canadian GAAP for publicly accountable enterprises or IFRS, and must be
    - (i) audited in accordance with Canadian GAAS and be accompanied by an auditor's report that expresses an unmodified opinion, identifies all financial periods presented for which the auditor has issued an auditor's report, and is in the form specified by Canadian GAAS for an audit of financial statements prepared in accordance with a fair presentation framework, and
    - (ii) prepared and signed by a person or company that is authorized to sign an auditor's report under the laws of a jurisdiction in Canada and that meets the professional standards of that jurisdiction;
 and
  - (b) a self-assessment of the accomplishments and the challenges faced during the year, which includes, but is not limited to
    - (i) a summary of developments in respect of section 8(j) of the Order,
    - (ii) a summary of Net Energy's business activity for the year and expansion plans that were implemented during the year,
    - (iii) a summary of new Contracts listed,
    - (iv) a report detailing the testing undertaken to ensure the adequacy of system safeguards, and
    - (v) a summary of staffing changes at Net Energy during the year.

**Other Reporting**

10. Before ceasing to operate, suspending, discontinuing or winding up all or a significant portion of its operations, or disposing of all or substantially all of its assets, Net Energy must:
- (a) provide the Commission at least 6 months' prior written notice; and

- (b) comply with any requirements the Commission may impose.
- 11. Net Energy will file concurrently with the Commission a copy of materials filed by Net Energy with any other regulatory body, except for those materials previously filed with the Commission.