

CP (2015-10)

Consultation Paper of the Cyprus Securities and Exchange Commission regarding trading in binary options

In the context of establishing effective arrangements and procedures for consultation with market participants regarding proposed changes in the regulatory framework, the Cyprus Securities and Exchange Commission ('the CySEC') is circulating this document for consultation.

CySEC has prepared this circular in order to inform the CIFs, that they must use trading platforms for reception and execution, or transmission, of orders, which, among others:

1. Provide adequate information to clients about binary options, so that there is full transparency.
2. Operate in a way that is fair to clients.

The proposed circular is attached as **Appendix 1**.

The CySEC invites you to submit your comments/suggestions, in word format, by Thursday December 31, 2015 to the electronic address supervision@cysec.gov.cy.

TO : **Cyprus Investment Firms**
FROM : **Cyprus Securities and Exchange Commission**
DATE : **December 14, 2015**
CIRCULAR NO. : **C0XX**
SUBJECT : **Trading in binary options**

[This circular refers to Cyprus Investment Firms which are providing services in relation to binary options ('the CIFs')]

The Cyprus Securities and Exchange Commission ('CySEC') wishes to inform the CIFs about the following:

A. Legislative framework

- 1.** Chapter C, Part V (Provisions for the protection of investors) of the Investment Services and Activities and Regulated Markets Law of 2009, as in force ('the Law') lays down conduct of business obligations when providing services to clients from CIFs.

B. Compliance with Law - Accepted Practices

- 2.** For compliance purposes with Chapter C , Part V of the Law, CIFs must use trading platforms for reception and execution, or transmission, of orders, which, among others:
 - i. Provide adequate information to clients about binary options, so that there is full transparency.
 - ii. Operate in a way that is fair to clients.
- 3.** For the purposes of ensuring compliance with the above provisions, the CySEC indicates in paragraphs 4-11 below, accepted practices applied in binary options trading platforms used by CIFs.

It is noted that these practices are not exhaustive and the CIFs are requested to establish and implement additional arrangements/procedures, having in mind the need for full transparency and protection of clients' interests.

4. Information on the identification of the underlying asset of the binary option

Providing clients with sufficient information regarding the identification of the underlying asset of the binary option, including the trading venue [e.g. WTI Crude Oil (Dec 15) NYMEX].

5. Information regarding bid and ask prices of the underlying asset of the binary option - Strike price of the binary option

- i. Providing to clients a continuous (per second) and smooth presentation of the flow of the bid/ask prices of the underlying asset of the binary option throughout the lifetime of the asset, such as those taken by the feed provider.
- ii. Disclosure of the bid/ask prices of the underlying asset of binary option in a prominent way in the trading platform. For example, disclosure of the bid/ask prices on the area where the exercise price is presented, in which clients may buy the binary option.
- iii. Adequate explanation/description of the bid/ask, and strike, prices in a prominent way in the trading platform (e.g. via a pop-up message).
- iv. Where the strike price differs from the average bid/ask price, a clear notification of it, as well as the deviation between the two prices, at absolute value and at least at the purchase of the binary option, on the area where the strike price is explained/described.
- v. In case where bid/ask prices are not available for certain underlying assets (e.g. index DAX and FTSE 100), presenting the last price of the binary option and clearly indicating the trading venue.
- vi. Publication of the feed provider details, e.g. in the pop-up where the bid/ask price is explained/described.

6. Information on the bid/ask, and/or last, prices, at the expiry of the binary option - Expiry price of the binary option

- i. Providing to clients the bid/ask, and/or last, prices at the expiry of the binary option.
- ii. Adequate explanation of the expiry price of the binary option and the methodology used to determine the expiry price.

In particular, among others:

- Reference to the relevant mathematical equation for the calculation of the expiry price [i.e. $(bid + ask / 2)$, $(last + bid + ask / 3)$].
- Explanation of the prices which constitute the expiry price (e.g. bid, ask, last). Where more than one prices are obtained by the feed provider at the second of the expiry of the binary option (e.g. 1/16/2015

10:11:01.424 am, bid 1.16394 ask 1.16404, 01/16/2015 10:11:01.885 am, bid 1.16395 ask 1.16404), clarification of the exact selection of data used.

- Explanation of any rounding of the expiry price of the binary option.
- Reference to the feed provider details.

iii. Maintaining historical records with the bid/ask, and/or last, prices at the expiry of the binary option, which they are accessible by clients.

iv. The above information is concentrated in a prominent way in the trading platform.

7. Explanation of the graphs presented to clients

The graphs presented in the trading platforms are accurate, clear and understandable to the average investor as to the describing illustrations. For example, when the buyout, or average bid/ask, prices are presented, a clear reference to the price presented and explanation of the graph.

8. Information on the availability of the binary option

- i. Possibility of entering buy orders of binary option (call and put), at any time and for any binary option that is available.
- ii. In the case of unavailability of purchasing a binary option (call and put), clear and visible information on this fact, as well as the circumstances/conditions under which this product is not available, before clients enter a buy order.

9. Buyout option of the binary option from a CIF

Providing clients a buyout option of the binary option from the CIF. Full and accurate explanation of the buyout methodology.

10. Cancellation option of the transaction in a binary option

Providing clients an option to cancel his transaction in binary options, within a reasonable time after its execution, indicating any conditions applied in relation to the frequency of its use. The length of this option is not less than five seconds after the purchase of the binary option.

11. Provision of services in relation to binary options that have investment features

Provision of services in relation to binary options that are constituted and traded in a manner similar to other derivatives and 'traditional' financial instruments included in the Law.

Binary options with duration of 30 and 60 seconds are not considered to fall under the above.

C. Establishment and implementation of appropriate arrangements/procedures

- 12.** CIFs are requested to immediately review their arrangements/procedures applied in the trading platforms that they use so as to ensure that these are in line and operated in accordance with the requirements of Chapter C, Part V of the Law and generally, with all the requirements of the Law. Where the CIFs are considered that additional arrangements/procedures are necessary to be established, are requested to do so immediately and not later than three (3) months from the date of this circular.

Sincerely,

Demetra Kalogerou
Chairman Cyprus Securities and Exchange Commission