ΕΠΙΤΡΟΠΗ ΚΕΦΑΛΑΙΑΓΟΡΑΣ ΚΥΠΡΟΥ
CYPRUS SECURITIES AND EXCHANGE COMMISSION

PRESS RELEASE

CySEC Consults to Impose National Measures to Restrict the Marketing, Distribution and Sale of Contracts for Differences

- *Proposal to adopt National Product Intervention Measures replicating ESMA's product intervention measures and to introduce a risk-based approach governing leverage limits*
- *Measures will enhance investor protection for all retail investors exposed to high-risk, speculative trading instruments*
- *Consultation follows a four year period of intense regulatory action concerning the CFD industry in Cyprus*

NICOSIA, 30 May 2019 - The Cyprus Securities and Exchange Commission ('CySEC') has today issued a consultation on imposing national measures to restrict the marketing, distribution and sale of contracts for difference ('CFDs').

Historically, investment firms have engaged in aggressive marketing techniques of CFDs, without providing adequate information on the risks involved in such speculative trading. Once such products were sold, retail investors were recurrently being allowed to trade with excessive levels of leverage (in some cases exceeding 1:500), incentivised to do so through the additional marketing of bonus promotions.

The majority of these transactions were found to result in firms' clients losing their entire invested capital and in some cases more than the invested capital resulting in negative balances on trading accounts. In addition, it was found that retail investors were likely to underestimate the risks involved.

Following close supervision of the industry by CySEC via a dedicated Supervisory Action Plan launched in 2015 and targeting the poor conduct of Cyprus Investment Firms ('CIFs') – many of whom traditionally passported investment services to the rest of the European Economic Area – CySEC has imposed record financial penalties on its regulated entities found to be in non-compliance with the legislation and has revoked 9 CFD licenses altogether.

In addition to the enforcement measures CySEC has introduced additional requirements since 2017. This included enforcing a predetermined leverage limit of 1:50 for all non-professional investors, a requirement to protect investors from negative balance protection; banning the provision of bonuses encouraging investors to invest in complex financial instruments, and guidelines for the proper management of conflicts of interest.

In order to manage firms' implementation of negative balance protection and ensure adequate investor protection, in February 2019, CIFs providing investment services in CFDs under a limited scope licence were required to revise their risk transfer arrangements. This meant that third parties which assume the market risk for client transactions have the responsibility for negative balances. CySEC also imposed additional capital requirements on CIFs providing CFDs, based on the geographic location of the entities to which the market risk is transferred.

Notwithstanding CySEC's own reforms and enforcement action, there continues to be legitimate concerns regarding adequate investor protection with CFD products. In line with the European Securities and Markets Authority's ('ESMA') temporary intervention measures – which are due to lapse for the final time in July 2019 – CySEC proposes to permanently introduce national product intervention measures ('NPIMs'), the majority of which replicate the ESMA measures.

These measures, which are subject of this consultation, include:

- Introducing a margin close out when a client's funds fall to 50% of the margin needed to maintain their open positions on their CFD account;
- Introducing a negative balance protection per account basis, so that retail clients cannot lose more than the total funds in their trading account;
- Prohibiting firms from offering cash or other inducements to encourage retail clients to trade; and,
- Requiring firms to provide standardised risk warnings informing potential clients the percentage of the firm's retail client accounts that make losses.

Furthermore, CySEC proposes a risk-based approach governing leverage restrictions on CFDs to proportionately address the risks arising from leverage.

In determining the suitability of CFD products during the customer due diligence process, each retail client must be categorised by the firm within a specific target market – either '*positive*' or '*negative*.' Retail clients who fall in the '*grey*' area of target market (fit neither within the positive target market nor within the negative target market) could be vulnerable to being offered leverage that exceeds their knowledge, financial position and risk appetite.

Accordingly, CySEC is proposing to introduce stricter leverage limits for retail clients falling within the 'grey area' of the target market, and affording slightly higher leverage limits for retail clients falling within the upper tier of the positive target market.

Proposed leverage limits are based on the volatility of the underlying asset(s), and the knowledge, wealth, risk appetite, objectives and needs of the respective retail client. Segmenting retail clients into three separate categories (plus retail clients falling within the negative target markets, who will not be allowed to be onboarded) will require careful CIF due diligence, onboarding and client categorisation processes.

CySEC is proposing to prohibit the marketing, distribution and sale of leveraged CFDs on crypto assets to retail clients, unless they fall within the upper tier of the positive target market to prevent exposure to excessive risk caused by the extreme volatility of the instrument.

Proposed leverage limits for each asset class compared with ESMA's temporary product intervention measures include:

- Retail clients falling within the "grey" target market (neither negative nor positive) will have extra protective measures via increased leverage limits:
  - 20:1 to trade major currency pairs (30:1 under ESMA);
  - 10:1 to trade non-major currency pairs (20:1 under ESMA);
  - 5:1 for "grey" to trade commodities other than gold (10:1 under ESMA);
  - 2:1 to trade individual equities (5:1 under ESMA);
  - 1:1 on crypto assets (2:1 under ESMA).

- Retail clients falling within the positive target market will be subject to the same leverage limit as under ESMA's measures, except for the case of CFDs on crypto assets:
  - 30:1 for major currencies (30:1 under ESMA)
  - 20:1 for non-major currencies (20:1 under ESMA)
  - 10:1 on commodities (10:1 under ESMA)
  - 5:1 on individual equities (5:1 under ESMA)
  - 1:1 on crypto assets (2:1 under ESMA).

- Retail clients falling within the upper tier of positive target market, subject to the satisfaction of customer due diligence and client suitability tests, will be able to access higher-yield trading strategies under slightly increased leverage limits:
  - 50:1 for major currencies (30:1 under ESMA)
  - 30:1 for non-major currencies (20:1 under ESMA)
  - 20:1 on commodities (10:1 under ESMA)
  - 10:1 on individual equities (5:1 under ESMA)
  - 2:1 on crypto assets (2:1 under ESMA).

In view of the fact that there is no longer activity in Binary Options in or from the Republic of Cyprus, as a consequence of the ESMA Decision on Binary Options, CySEC intends to adopt permanent National Product Intervention Measures on Binary Options, which will be the same as ESMA's measures, without any pubic consultation on the subject matter. An official statement will be issued once the measures are formally adopted.

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Demetra Kalogerou, Chair of CySEC, said: *"Following over four years of intense regulatory action by CySEC, the standard and conduct of Cyprus Investment Firms marketing, selling and distributing retail contracts for difference has increased significantly. Temporary product intervention measures set across Europe have supported CySEC's own efforts to enhance investor protection. As this guidance is transposed into law alongside additional national measures and restrictions set by CySEC, our consultation with investors and the industry will provide opportunity for feedback on what we see as the fundamental new rules of engagement. Whilst the consumer demand for high risk, speculative trading products shows no sign of decreasing in Europe, Cyprus Investment Firms must continue reforming their business models to ensure investors are adequately protected."*

Consultation process:

Interested parties may submit their comments to the CySEC Policy Department by email at policy@cysec.gov.cy .

The submission of comments should be made no later than 14 June 2019 .

The subject of the email should have the following form:

"*Consultation Paper (2019 - 02) – [insert the Name of Organisation, Legal or Natural Person submitting the comments or views]*"

ENDS.

Notes to editors: Appendix of full proposed leverage limits:

Type of Underlying Asset	CySEC Proposal		ESMA's Threshold	
	Initial Margin Protection	Leverage Limit	Initial Margin Protection	Leverage Limit
Major Currency Pairs	5%	20:1	3,33%	30:1
Non-major currency pairs, gold and major indices	10%	10:1	5%	20:1
Commodities other than gold and non-major equity index	20%	5:1	10%	10:1
For individual equities and other reference values;	50%	2:1	20%	5:1

Crypto assets	100%	1:1	50%	2:1

Retail clients falling within the positive target market should pay the following initial margin protection of the notional value of the CFD (i.e. leverage limits):

Type of Underlying Asset	CySEC Proposal		ESMA Limits	
	Initial Margin Protection	Leverage Limit	Initial Margin Protection	Leverage Limit
Major Currency Pairs	3,33%	30:1	3,33%	30:1
Non-major currency pairs, gold and major indices	5%	20:1	5%	20:1
Commodities other than gold and non-major equity index	10%	10:1	10%	10:1
For individual equities and other reference values;	20%	5:1	20%	5:1
Crypto assets	100%	1:1	50%	2:1

Retail clients falling within the upper tier of positive target market should pay the following initial margin protection of the notional value of the CFD (i.e. leverage limits):

Type of Underlying Asset	CySEC Proposal		ESMA Limits	
	Initial Margin Protection	Leverage Limit	Initial Margin Protection	Leverage Limit
Major Currency Pairs	2%	50:1	3,33%	30:1
Non-major currency pairs, gold and major indices	3,33%	30:1	5%	20:1
Commodities other than gold and non-major equity index	5%	20:1	10%	10:1
For individual equities and other reference values;	10%	10:1	20%	5:1
Crypto Assets	50%	2:1	50%	2:1