

CSA Multilateral Notice of Publication***Regulation 91-102 respecting Prohibition of Binary Options******Policy Statement to Regulation 91-102 respecting Prohibition of Binary Options***

September 28, 2017

Introduction

We, the securities regulatory authorities in all Canadian jurisdictions other than British Columbia (collectively, the **Participating Jurisdictions**), are implementing the following:

- *Regulation 91-102 respecting Prohibition of Binary Options* (the **Regulation**); and
- *Policy Statement to Regulation 91-102 respecting Prohibition of Binary Options* (the **Policy Statement**).

In this Notice, the Regulation and the Policy Statement are referred to collectively as the **Binary Options Instrument**.

In some jurisdictions, government ministerial approvals are required for the implementation of the Regulation. Provided all necessary approvals are obtained, the Binary Options Instrument will come into force on December 12, 2017.

The British Columbia Securities Commission is not an authority implementing the Binary Options Instrument. Please see BC Notice 2017/02 – *Binary Options* for more information regarding the regulation of binary options in BC.

Substance and Purpose

The purpose of the Binary Options Instrument is to protect would-be investors from becoming victims of binary options fraud and from an illegal promotion of extremely high risk products. We believe the Regulation will achieve this goal by raising awareness among investors that the sale of these products is illegal and by disrupting the distribution of these products, including its facilitation through payment processing and advertising. To this end, the Regulation explicitly prohibits advertising, offering, selling or otherwise trading a binary option with or to an individual.

Summary of the Regulation

The Regulation prohibits advertising, offering, selling or otherwise trading a binary option having a term to maturity of less than 30 days with or to:

- an individual, and
- a person that is created, or is used, solely to trade a binary option.

The Regulation sets out a definition of “binary option” that is intended to capture a range of products that are commonly called binary options, or that are similar to products that are commonly called binary options, regardless of how they are named.

Background

Binary options

Binary options are based on the outcome of a yes/no proposition. If the outcome is yes, the buyer wins or is “in-the-money”. If the answer is no, the buyer loses or is “out-of-the-money” and loses all, or nearly all, of their investment. The yes/no proposition is structured on the performance of an underlying interest referenced in the contract – for example, a change in the value of a currency, commodity, stock index, or listed security – or the occurrence of a specified event in connection with an underlying interest – for example, the outcome of an election or a change in a benchmark interest rate. The time or time period specified in the contract for determining whether the predetermined condition (i.e., the outcome of the yes/no proposition) or conditions are met can be very short, sometimes hours or even minutes. The buyer either:

- is entitled to receive a predetermined fixed amount if the predetermined condition or conditions are met, i.e., the buyer wins or is “in-the-money”, or
- loses all or nearly all of the amount that was paid to enter into the binary option if the predetermined condition or conditions are not met, i.e., the buyer loses or is “out-of-the-money”.

Binary options fraud

We are concerned by the large number of complaints received regarding the marketing of products commonly called “binary options” to individuals. Binary options are also called a variety of other names, including but not limited to:

- all-or-nothing options,
- asset-or-nothing options,
- bet options,
- cash-or-nothing options,
- digital options,
- fixed-return options, and
- one-touch options.

All contracts or instruments, however named, marketed or sold that meet the definition of a binary option are prohibited under the Regulation.

A significant number of the complaints and inquiries received by CSA members concern online

binary options platforms. These platforms operate as unregistered dealers, are typically located off-shore, and promise quick and high-yielding returns from trading binary options. On some platforms, trading may actually take place but it is typically extremely difficult and often impossible to win on the bet (because the platform controls the odds and often the reference value of the underlying interest). In some cases, even if an individual theoretically does win, the winnings may appear as a credit on a trading account on the platform but the investor's money is not transferred or returned. In many other cases, no trading actually takes place and the operation is purely a fraud set up to take money from individuals, including through cash advances processed through the target's credit card. Once a victim has lost their money, it is almost impossible to recuperate their losses.

No individuals or firms are registered to sell binary options in Canada

The Regulation prohibits advertising, offering, selling and otherwise trading binary options to an individual and to a person that was created, or is solely used, to trade binary options.

We consider a person to be trading in securities or derivatives in a local jurisdiction if that person offers or solicits transactions in securities or derivatives to persons in that local jurisdiction, including through a website or other electronic means.

Offering investment services or products to persons, whether by telephone, online or in-person, is a regulated activity. It is illegal to offer securities or derivatives, including binary options, whether or not subject to the Regulation, without being registered as a dealer. There are only limited and narrow exceptions to the registration requirement for transactions with highly sophisticated investors. We emphasize that no offering of these products, including by a broker, dealer or platform, has been authorized anywhere in Canada. Many of these products and the platforms selling them have been identified as vehicles to commit fraud.

Investing through unregistered offshore platforms or dealers can be risky and is a common red flag for investment fraud. Registration as a dealer is an important safeguard for investors, helping to ensure the character, proficiency and solvency of the dealer and typically requiring the registered dealer to assess the suitability of an investment for an investor. We encourage all investors to visit aretheyregistered.ca to check the registration of any person offering investment products, including binary options, to Canadians. Anyone who has invested with, or has concerns about, a binary options trading platform should contact their local securities regulator. We also encourage all investors to visit binaryoptionsfraud.ca.

Summary of Written Comments Received

The Regulation was published for comment as Draft *Regulation 91-102 respecting Prohibition of Binary Options* (the **Draft Regulation**) on April 26, 2017 in all CSA jurisdictions except BC. The public comment period for the Draft Regulation expired on May 29, 2017 in Alberta and Québec, June 28, 2017 in Manitoba and Saskatchewan, and July 28, 2017 in all other CSA jurisdictions except BC.

We received eight comment letters on the Draft Regulation. A list of those who submitted comments as well as a chart summarizing the comments received and our responses is attached

as Annex A to this Notice. Copies of the comment letters can be found on the websites of the Alberta Securities Commission, Autorité des marchés financiers, and Ontario Securities Commission.

Summary of Changes

We have made certain non-significant changes to the Regulation in response to the comments received. We have also made several non-significant changes to the Policy Statement to provide further guidance on the types of contracts we intend and do not intend to capture under the Regulation.

Questions

Please refer your questions to any of:

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ANNEX A

Summary of Comments and CSA Responses on *Draft Regulation 91-102 respecting Prohibition of Binary Options*

<u>Section Reference</u>	<u>Summary of Issues/Comments</u>	<u>Response</u>
GENERAL COMMENTS		
General Comments	<p>Commenters generally supported the efforts of the CSA to help protect would-be investors from binary options fraud and generally strengthen the integrity of, and public confidence in, the financial sector, including by ensuring that products cannot be sold to investors through unauthorized mechanisms.</p> <p>One commenter noted that certain investors mistake the current unlawful activity for that of regulated brokers in Canada, and that the reputation of the financial and brokerage industry is, therefore, indirectly at stake.</p>	No change. We thank the commenters for their submissions.
	Commenters had mixed views on binary options:	We thank the commenters for their submissions.
	<ul style="list-style-type: none"> One commenter stated that binary options are high risk and not a get rich quick scheme, suggesting that the CSA should not ban binary options for all investors because some people have lost money. 	
	<ul style="list-style-type: none"> Another commenter urged that binary options are, by design, harmful for investors, particularly retail investors. The commenter stated that firms should not be allowed to offer binary options to the public, and particularly not to retail investors. 	

	<ul style="list-style-type: none"> • One commenter submitted that the offering of binary options does not enhance any investor portfolio, nor does it enhance fair and efficient capital markets. • Another commenter submitted that non-fraudulent binary options products can be used to offset an existing risk or economic exposure or to speculate on market volatility – for example, to hedge or speculate on very short term market volatility created by the release of specific major economic figures. 	
<p>Will the Draft Regulation accomplish the intended purpose?</p>	<p>Commenters generally noted that those operating fraudulent online binary options platforms are unlikely to comply with the Draft Regulation.</p> <p>Two commenters stated that the Draft Regulation will not end the illegal activity but may interfere with current “legal” institutional binary options trading taking place in the Canadian market.</p> <p>One commenter submitted that the only market participants that will comply with the Draft Regulation, such as the large institutional dealers, are already complying with all applicable securities laws and regulations.</p>	<p>No change. The Regulation is one aspect of the CSA’s multi-pronged effort to combat binary options fraud, and we have already seen positive outcomes from this rule-making project.</p>
	<p>Two commenters submitted that the policy objectives could be met with a narrowed scope, and that products traded on a recognized exchange or cleared by a recognized clearing agency or clearing house, or financial instruments legally traded on certain US exchanges should be excluded from the prohibition.</p>	<p>No change. It is currently our view that binary options should not be permitted to be sold to individuals by a registered dealer or regulated exchange.</p>

	One commenter submitted that the detailed regulatory oversight regimes applicable in each Participating Jurisdiction has proven to be effective with respect to other types of instruments, and that any financial product, and not only binary options, that is offered illegally to Canadian investors poses a threat to investors' protection.	No change. It is currently our view that binary options should not be permitted to be sold to individuals by a registered dealer or regulated exchange.
Investor protection	One commenter submitted that, by prohibiting trading of binary options with a maturity of less than 30 days, the regulator is meeting its mandate to provide protection to investors from unfair, improper or fraudulent practices and to foster fair and efficient capital markets.	No change. We thank the commenter for their submission.
	One commenter noted that many of the investor protection-related concerns regarding binary options are also present regarding leveraged retail forex and CFDs, including regarding pricing transparency, and queried whether other leveraged derivatives products sold to retail investors should also be covered in this rule-making project.	No change. The focus of the Regulation is specifically on the fraud being perpetrated by unregulated, online platforms providing primarily – to date – binary options.

Alternative approaches to accomplishing the policy objectives		<p>Commenters pointed to other tools to deter and eliminate fraud relating to binary options, either in support of the Draft Regulation or instead of the Draft Regulation.</p> <p>One commenter submitted that efforts to attack the bad actors rather than the financial instrument, and that limit demand for the illegal product (e.g., allowing registered firms and exchanges to offer legitimate binary options as a legal alternative) would more effectively protect the Canadian public and reduce the fraud than attempting to ban a financial product.</p>	<p>We note that the Regulation is one aspect of the CSA's multi-pronged effort to combat binary options fraud, and that we have already seen positive outcomes from this rule-making project.</p>
		<p>Four commenters generally felt that fraudulent binary options platforms and their offerings should be dealt with differently than "legitimate" binary options offered by a registered dealer or a recognized exchange, as in the U.S. and certain other jurisdictions.</p>	<p>No change. It is currently our view that binary options will not be permitted to be sold to individuals by a registered dealer or regulated exchange.</p>
	Enforcement	<p>One commenter urged that the only effective means of influencing the fraudulent online platforms is through enforcement actions.</p> <p>Another commenter sought more emphasis in the Draft Regulation on utilizing enforcement tools and coordinated enforcement action with other jurisdictions to deter and eliminate fraud associated with binary options.</p>	<p>No change. The Regulation is one aspect of the CSA's multi-pronged effort to combat binary options fraud, and we have already seen positive outcomes from this rule-making project.</p>

	Investor warnings and investor education	Two commenters stated that the only way to prevent online fraud is to tell Canadians about this “trading” scam as well as the related “we help recover your money” scam, and urged regulators to continue investor warnings and investor education programs – pointing to other CSA efforts, including: the website www.binaryoptionsfraud.ca , holding investor information seminars, and advertising warning of the dangers of buying binary options from online platforms.	No change. The Regulation is one aspect of the CSA’s multi-pronged effort to combat binary options fraud.
	Coordinating with distribution and facilitation service providers	One commenter noted that major credit card companies have recently taken steps to limit the availability of funding to unregistered providers of binary options. The commenter submitted that the Participating Jurisdictions should also work with search engine providers to limit online advertising of illegal services to Canadian consumers.	No change. The Regulation is one aspect of the CSA’s multi-pronged effort to combat binary options fraud.
	Regulating binary options as fraud	Two commenters recommended the RCMP be involved in stopping online binary options fraud, by handling investigations, shutting down websites and prosecuting platforms in coordination with international law enforcement agencies.	No change. The Regulation is one aspect of the CSA’s multi-pronged effort to combat binary options fraud.
	Regulating binary options as gambling	One commenter submitted that fraudulent binary options should be treated as gambling activity, regulated by the applicable gambling authority in each province and subject to the Criminal Code, with enforcement by the RCMP.	No change. We are of the view that binary options are securities and/ or derivatives in each Participating Jurisdiction and therefore that regulating the advertising, offering, selling and otherwise trading of binary options is within the CSA’s regulatory jurisdiction and mandate.

	Permitting binary options to be offered by a registered (or exempt) dealer	Two commenters recommended that, if the CSA proceeds with the Draft Regulation, that the rule should provide for a general exception for selling binary options through a registered or exempt dealer. One commenter recommended that the CSA allow registered, IIROC-regulated firms to offer these products to all investors (including both retail and sophisticated investors), in order to: ensure the protection of the public against unfair, abusive and fraudulent practices; apply the concepts of investment suitability; and apply disclosure obligations to allow clients to understand the product and the significant risks involved.	No change. It is currently our view that binary options will not be permitted to be sold to individuals by a registered dealer.
	Permitting binary options to be offered on a recognized (or exempt) exchange or cleared by a recognized clearing agency or clearing house	Two commenters recommended that the CSA permit binary options to be offered to individuals on a recognized exchange. One commenter recommended that the CSA permit a registered dealer to offer binary options traded on a recognized exchange, or cleared by a recognized clearing agency or clearing house, noting the level of CSA oversight over a recognized exchange and a recognized clearing agency.	No change. It is currently our view that binary options will not be permitted to be sold to individuals through a recognized exchange or cleared by a recognized clearing agency.
s. 1 – Definition			
Definition of “binary option”	Several commenters suggested that the definition of “binary option” is too broad, as it may prohibit:		
	<ul style="list-style-type: none">the offering to an individual of an instrument otherwise duly listed on a recognized exchange or cleared by a recognized clearing agency;	No change. The Regulation is intended to prohibit the advertising, offering, selling and otherwise trading of a binary option to an individual, regardless of whether it is listed on a recognized exchange or cleared by a recognized clearing agency.	

	<ul style="list-style-type: none"> conventional options with a term of less than 30 days that are used by individuals; 	No change. A conventional option would not become a prohibited “binary option” simply because its term to maturity is less than 30 days.
	<ul style="list-style-type: none"> legitimate binary option transactions executed by institutional and sophisticated investors; 	No change. The Regulation is intended to prohibit the advertising, offering, selling and otherwise trading of a binary option to an individual, including an individual that is a sophisticated investor.
	<ul style="list-style-type: none"> genuine non-fraudulent binary options that have been offered for many years by regulated firms dealing over-the-counter in Europe and Japan, or in the United States on exchanges. 	No change. The Regulation is intended to prohibit the advertising, offering, selling and otherwise trading of all binary options to individuals.
	<ul style="list-style-type: none"> binary contracts currently being legitimately sold to sophisticated individuals, including products described in the ISDA 2005 Barrier Option Supplement to the 1998 FX and Currency Option Definitions¹. 	Change made. After follow-up consultations with commenters, we have revised the definition of “binary option” to mitigate against the Regulation capturing some products that were not intended to be caught. We believe that some of the products identified to us would not be caught by the definition, while other products – including some identified in the ISDA 2005 Barrier Option Supplement – would be caught. Information available to us indicates that individuals are not actively trading products under the ISDA 2005 Barrier Option Supplement.
	One commenter submitted that the definition may be too narrow, as it may not capture all types of product that present similar concerns and it may be too easy for a fraudulent online platform to work around.	No change. The revised definition of “binary option” reflects a balancing of efforts intended to focus only on the products we intend to prohibit to be traded with individuals.

¹ Available at: <https://www.newyorkfed.org/medialibrary/microsites/fxc/files/2005/fxc051206a.pdf>.

	One commenter submitted that the words, “a lesser amount or” should be deleted from section 1(b) to help mitigate the risk that other products, including those that do not involve an “all or nothing” approach, would be captured under this definition.	Change made. Paragraph (b) of the definition of “binary option” has been revised.
	One commenter submitted that the scope of the Draft Regulation should be limited by the scope of contracts set out under the various <i>Derivatives: Product Determination</i> rules ² .	No change. A number of the exclusions in the <i>Derivatives: Product Determination</i> rules are not appropriate or are not relevant to the Regulation.
s. 2 – Trading binary options with an individual prohibited		
Exclusion for offering binary options to sophisticated investors	One commenter submitted that only an unsophisticated individual is in need of the protection of the Draft Regulation, and that sophisticated individuals have the ability to analyze and discern the risks inherent in binary option transactions. The commenter noted that “accredited investors” are considered sufficiently sophisticated that securities can be sold to them without a disclosure document.	No change. It is currently our view that binary options will not be permitted to be sold to individuals, including individuals that are “accredited investors”.
s. 3 – Trading binary options with a person other than an individual prohibited		
Not necessary	Two commenters submitted that proposed section 3 should be removed, because any retail investor that has the means to create a company or a trust in order to circumvent a trading ban should be considered a sophisticated investor, and that such an individual should not need the protection of the Draft Regulation.	No change. It is currently our view that binary options will not be permitted to be sold to individuals, including through a company or other entity created, or used, solely to trade a binary option.

² Manitoba Securities Commission Rule 91-506 *Derivatives: Product Determination*; Ontario Securities Commission Rule 91-506 *Derivatives: Product Determination*; Québec Regulation 91-506 respecting *Derivatives determination*; and Multilateral Instrument 91-101 *Derivatives: Product Determination*.

Impractical	One commenter stated that proposed section 3 would be impractical and difficult to implement, as the dealer would need to look behind its counterparty to determine whether it was created, or is primarily used, to trade a binary option for an individual. The broad wording of the provision means the determination would need to be made in respect of all or almost all of a dealer's counterparties.	Change made. Section 3 has been revised to better facilitate implementation by entities that comply with all applicable securities legislation in providing legitimate, non-fraudulent contracts and instruments to counterparties that are not individuals and that are not structured to evade the Regulation.
s. 4 – Binary options having a term to maturity of 30 days or longer		
Term to maturity of 30 days or longer	Commenters generally queried the focus on binary options having a term to maturity shorter than 30 days. One commenter requested an explanation for the 30-day term to maturity in the prohibition.	No change. We have reviewed the products being illegally provided on unregistered online platforms and are satisfied that the minimum 30-day term to maturity period is appropriate to balance our objectives.
	Two commenters submitted that all binary options, regardless of duration, present similar concerns and therefore that the Draft Regulation should not be limited to only binary options of 30 days or less.	No change. We feel that the minimum 30-day term to maturity strikes an adequate balance between banning the types of quick-turnover products that invite fraudulent activity and not banning legitimate trading in other types of instruments.
	One commenter requested clarification on the application of the 30-day term to maturity in the prohibition.	Change made. Section 4 has been revised to exclude a binary option having a term to maturity of 30 days or longer.
	One commenter stated that the 30-day minimum expiry time is inappropriate, as markets can move very quickly.	No change. The Regulation is designed to prohibit short-term binary options.

	One commenter suggested that the 30-day limitation may preclude a trader from closing out a position through an offsetting trade with less than 30 days to expiration, thereby limiting the trader's ability to take profits or limit losses.	No change. The prohibition applies only to a “binary option”, as defined in the Regulation; therefore, the minimum 30-day term to maturity exclusion serves only to carve out from the prohibition those contracts that (i) meet the definition of “binary option”, and (ii) have a term to maturity of 30 days or longer. The minimum 30-day term to maturity exclusion in no way affects a trader’s ability to trade in, or close out a position in, a contract that is not a binary option.
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List of Commenters:

1. Canadian Advocacy Council for Canadian CFA Institute Societies
2. Canadian Market Infrastructure Committee
3. Canadian Foundation for Advancement of Investor Rights
4. Investment Industry Association of Canada
5. Investor Advisory Panel of the Ontario Securities Commission
6. North American Derivatives Exchange, Inc.
7. TMX Group, on behalf of the Bourse de Montréal Inc. and the Canadian Derivatives Clearing Corporation
8. Tyson G.