

CSA Notice and Request for Comment

Proposed National Instrument 91-102 *Prohibition of Binary Options* and Related Proposed Companion Policy

April 26, 2017

Introduction

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

- Proposed National Instrument 91-102 *Prohibition of Binary Options* (the **Instrument**);
- Proposed Companion Policy 91-102 *Prohibition of Binary Options* (the **CP**).

In this Notice, the Instrument and the CP are referred to collectively as the **Proposed Instrument**.

We are issuing this Notice to solicit comments on the Proposed Instrument. We welcome all comments on the Proposed Instrument and have also included specific questions in the Comments section below.

While the British Columbia Securities Commission is not an authority publishing the Proposed Instrument under this Notice, it anticipates that, subject to receiving the necessary approvals, it will, in the near future, publish for comment a proposed instrument that will be consistent with the Proposed Instrument described in this Notice.

The public comment period expires

- May 29, 2017 in Alberta and Québec,
- June 28, 2017 in Manitoba and Saskatchewan, and
- July 28, 2017 in all other Participating Jurisdictions.

We encourage commenters in all Participating Jurisdictions, to the extent possible, to provide their comments by May 29, 2017.

Certain Participating Jurisdictions are considering implementing a final rule in advance of other Participating Jurisdictions. However, we anticipate that the instrument that will ultimately be

adopted in all CSA jurisdictions will be fully harmonized – e.g., through harmonizing amendments, where necessary.

Background

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

By publishing the Proposed Instrument, we are not suggesting that current offerings of binary options in Canada are legal. Many of these products and the platforms selling them have been identified as vehicles to commit fraud. We emphasize that no offering of these products, including by a broker, dealer or platform, has been authorized in Canada. All current offerings in Canada are therefore illegal, with only limited and narrow exceptions for transactions with highly sophisticated investors. Nevertheless, some persons are using misleading information to promote these products as legal and legally offered.

It is our intention that the Proposed Instrument will make it explicitly clear that these products may not be advertised, offered, sold or otherwise traded to an individual in Canada.

AMF Proposal

On February 1, 2017, the Québec Autorité des marchés financiers (AMF) proposed an amendment¹ to the Québec *Derivatives Regulation* that was intended to prohibit the offering of a binary option with a maturity of less than 30 days to an individual (the [AMF Proposal](#)). The Participating Jurisdictions are proposing the Proposed Instrument as a means of implementing a prohibition in line with that set out in the AMF Proposal. The AMF is considering withdrawing the AMF Proposal and instead recommending the adoption of the Proposed Instrument.

Binary options fraud

We are concerned by the growing 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 this definition will be prohibited under the Proposed Instrument.

A significant number of the complaints and inquiries received by CSA members concern online binary options platforms. These unregistered platforms, typically located off-shore, 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 their 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.

¹ Draft Regulation to amend the Derivatives Regulation, February 1, 2017. The Notice, Draft Regulation and comments letters received in response to the Draft Regulation are available on the AMF website (www.lautorite.qc.ca).

Offering investment services or products to persons or companies in Canada, whether by telephone, online or in-person, is a regulated activity. It is illegal to offer investment services or products, including binary options not subject to the Proposed Instrument, in Canada without being registered as a dealer, with only limited and narrow exceptions for transactions with highly sophisticated investors.

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 suitability of the investment, and the character, proficiency and solvency of the dealer. The CSA encourage all investors to visit aretheyregistered.ca to check the registration of any person or company 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.

Current regulation of binary options

We remind market participants that binary options, even binary options that are not subject to the Proposed Instrument, are derivatives and/or securities in each jurisdiction of Canada and that persons or companies advertising, offering, selling or otherwise trading such products to persons or companies in Canada are subject to securities legislation in Canada, including for example, anti-fraud provisions and requirements respecting registration, market conduct, and disclosure. Furthermore, in jurisdictions of Canada where binary options are regulated as securities, trading a binary option may be a distribution subject to the prospectus requirement.

In Québec, under the qualification regime, any person that wishes to create or market a derivative is required to apply to the AMF for qualification before the derivative is offered to the public. A qualified person may only market derivatives that have been duly authorized by the AMF as listed in its qualification decision or in a specific decision following an application by the qualified person. In addition, the qualified person must offer derivatives to the public through a registered dealer, or register with the AMF as a dealer.

The CSA consider a person or company to be trading in securities or derivatives in a local jurisdiction if that person or company offers or solicits trades of securities or derivatives to persons or companies in that local jurisdiction, including through a website or other electronic means.

Substance and Purpose of the Proposed Instrument

The purpose of the Proposed Instrument is to protect would-be investors from becoming victims of binary options fraud and from becoming victims of an illegal promotion of an extremely high risk product, by raising awareness among investors that these products are illegal and by disrupting the advertising and facilitation of these products. To this end, the Proposed Instrument will explicitly prohibit advertising, offering, selling or otherwise trading a binary option to an individual.

Summary of the Proposed Instrument

Prohibition

The Proposed Instrument prohibits advertising, offering, selling or otherwise trading a binary option with or to an individual. To prevent a party that offers a binary option from avoiding the prohibition by having their proposed client create a corporation or other type of entity to trade binary options, the Proposed Instrument also prohibits advertising, offering, selling or otherwise trading a binary option with or to any other person or company that is created, or is primarily used, to trade a binary option.

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

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 currency, commodity, stock index, or share – or the occurrence of a specified event referenced in the contract – 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 or conditions are met is often very short, sometimes hours or even minutes. The buyer either

- is entitled to receive a fixed amount if the predetermined condition is met, i.e., the buyer wins or is “in-the-money”, or
- loses all or nearly all of the amount paid if the predetermined condition is not met, i.e., the buyer loses or is “out-of-the-money”.

Anticipated Costs and Benefits

The Proposed Instrument is directed at prohibiting trading a binary option with an individual. Individuals are the primary targets of fraudulent binary options platforms, and non-fraudulent binary options also pose significant risks to individuals. The Proposed Instrument is intended to help protect would-be investors from binary options fraud, by prohibiting advertising, offering, selling and otherwise trading a binary option to an individual. It is also intended to reduce investor confusion about this form of product by making it clear that binary options are prohibited for individuals.

Potential offerors of binary options will be prohibited from offering these products to individuals if the time or time period specified for determining whether the predetermined condition or conditions are met is less than 30 days from the date the binary option is entered into. However, we do not believe that the prohibition will have a negative impact on investors’ access to necessary financial products.

We believe that the benefits to the market of reducing fraud and investor loss relating to binary options outweigh any costs of the Proposed Instrument.

Contents of Annexes

The following annexes form part of this CSA Notice:

- Annex A – Proposed National Instrument 91-102 *Prohibition of Binary Options*,
- Annex B – Proposed Companion Policy 91-102 *Prohibition of Binary Options*, and
- Annex C – Local Matters.

Comments

In addition to your comments on all aspects of the Proposed Instrument, we also seek specific feedback on the following questions:

1. Does the proposed definition of “binary option” capture contracts or instruments that should not be captured? If so, please specify the types of contracts or instruments that should not be captured and on what basis they would be captured.
2. The Proposed Instrument applies to binary options where the time period specified in the binary option for determining whether the predetermined condition or conditions are met is less than 30 days from the date the binary option is entered into. Is this time period appropriate? Please specify why or why not.
3. Staff considered a variety of options that would prevent circumvention of the binary options trading ban. These included provisions that would capture indirect trading by an individual through a company, trust or other entity. As currently drafted, the Proposed Instrument includes an anti-avoidance provision that would ban trading binary options with a person or company that is created, or primarily used, to trade binary options. We believe this approach captures our intent to prohibit attempted work-arounds of the binary options trading ban without increasing the complexity of the rule. Is the proposed provision unambiguous and clear, or should the scope of this provision be modified, for example, to more specifically extend to any person, company or other entity wholly-owned or controlled by an individual?
4. Do you believe the Proposed Instrument will accomplish the intended purpose of proposing it, as set out in this Notice?

Please provide your comments in writing by

- May 29, 2017 if responding to the Alberta Securities Commission or the Québec AMF,
- June 28, 2017 if responding to the Manitoba Securities Commission or the Financial and

Consumer Affairs Authority of Saskatchewan, and

- July 28, 2017 if responding to any other Participating Jurisdiction.

We cannot keep submissions confidential because securities legislation in certain provinces requires publication of a summary of the written comments received during the comment period. In addition, all comments received will be posted on the websites of each of the Alberta Securities Commission at www.albertasecurities.com, the Autorité des marchés financiers at www.lautorite.qc.ca and the Ontario Securities Commission at www.osc.gov.on.ca. Therefore, you should not include personal information directly in comments to be published. It is important that you state on whose behalf you are making the submission.

Thank you in advance for your comments.

Please address your comments to each of the following:

Alberta Securities Commission
 Autorité des marchés financiers
 Financial and Consumer Services Commission (New Brunswick)
 Financial and Consumer Affairs Authority of Saskatchewan
 Manitoba Securities Commission
 Nova Scotia Securities Commission
 Nunavut Securities Office
 Ontario Securities Commission
 Office of the Superintendent of Securities, Newfoundland and Labrador
 Office of the Superintendent of Securities, Northwest Territories
 Office of the Yukon Superintendent of Securities
 Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

If you are submitting your comments prior to May 29, 2017, please send your comments **only** to the following addresses. Your comments will be forwarded to the remaining jurisdictions:

M^e Anne-Marie Beaudoin
 Corporate Secretary
 Autorité des marchés financiers
 800, rue du Square-Victoria, 22^e étage
 C.P. 246, tour de la Bourse
 Montréal (Québec) H4Z 1G3
 Fax: 514-864-6381
consultation-en-cours@lautorite.qc.ca

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

If you are submitting your comments after May 29, 2017 but prior to July 28, 2017, please send your comments **only** to the following address. Your comments will be forwarded to the remaining jurisdictions:

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

Questions

Please refer your questions to any of:

Lise Estelle Brault
Co-Chair, CSA Derivatives Committee
Senior Director, Derivatives Oversight
Autorité des marchés financiers
514-395-0337, ext. 4481
lise-estelle.brault@lautorite.qc.ca

Kevin Fine
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Director, Derivatives Branch
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416-593-8109
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Alberta Securities Commission
403-355-2804
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Financial and Consumer Services
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506-643-7202
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Financial and Consumer Affairs Authority
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306-787-5842
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Nova Scotia Securities Commission
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ANNEX A

PROPOSED NATIONAL INSTRUMENT 91-102 *PROHIBITION OF BINARY OPTIONS*

Definition

1. In this Instrument, “binary option” means a contract or instrument that provides for only
 - (a) a fixed amount if the underlying interest referenced in the contract or instrument meets one or more predetermined conditions, and
 - (b) a lesser amount or zero if the underlying interest referenced in the contract or instrument does not meet one or more predetermined conditions.

Trading binary options with an individual prohibited

2. No person or company may advertise, offer, sell or otherwise trade a binary option with or to an individual.

Trading binary options with a person or company other than an individual prohibited

3. No person or company may advertise, offer, sell or otherwise trade a binary option with or to a person or company that is not an individual and that is created, or is primarily used, to trade a binary option.

Binary options of 30 days or longer

4. Sections 2 and 3 do not apply in respect of a binary option if the time specified in the binary option for determining whether one or more predetermined conditions is met is 30 days or more from the date the binary option is entered into.

Exemption – general

5. (1) Except in Québec, the regulator or the securities regulatory authority may grant an exemption from this Instrument, in whole or in part, subject to such conditions or restrictions as may be imposed in the exemption.
- (2) Despite subsection (1), in Ontario, only the regulator may grant an exemption.
- (3) Except in Alberta, Ontario and Saskatchewan, an exemption referred to in subsection (1) is granted under the statute referred to in Appendix B of National Instrument 14-101 *Definitions* opposite the name of the local jurisdiction.

Effective date

6. This Instrument comes into force on [●].

INCLUDES COMMENT LETTERS

ANNEX B

PROPOSED COMPANION POLICY 91-102 *PROHIBITION OF BINARY OPTIONS*

Introduction

The purpose of National Instrument 91-102 *Prohibition of Binary Options* (the **Instrument**) is to help protect would-be investors from binary options fraud.

The purpose of this Companion Policy is to state the view of the members of the Canadian Securities Administrators (the “CSA” or “we”) on various matters related to the Instrument.

We are concerned by complaints we have received regarding the marketing of products commonly called “binary options” to individuals. Many of these products and the platforms selling them have been identified as vehicles to commit fraud. Some persons have used misleading information to promote these products as legal and legally offered, despite not being authorized to offer these products to individuals in Canada. The Instrument explicitly prohibits advertising, offering, selling or otherwise trading a binary option (as defined in the Instrument) with or to an individual.

The CSA consider a person or company to be trading in securities or derivatives in a local jurisdiction if that person or company offers or solicits trades of securities or derivatives to persons or companies in that local jurisdiction, including through a website or other electronic means.

Definitions and interpretation

Unless defined in the Instrument or this Companion Policy, terms used in the Instrument and in this Companion Policy have the meaning given to them in securities legislation, including in National Instrument 14-101 *Definitions*. “Securities legislation” is defined in National Instrument 14-101 *Definitions*, and includes statutes and other instruments related to both securities and derivatives.

Interpretation of terms used or defined in the Instrument

Section 1 – Definition of “binary option”

The defined term “binary option” is intended to capture a range of products that are, or are similar to, products that are commonly called binary options, regardless of how they are named. Binary options are sometimes 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”.

Binary options are based on the outcome of a yes/no proposition, expressed as whether an underlying asset, event or value meets one or more predetermined conditions specified in the contract or instrument, at or during the time or time period specified in the contract or instrument. The specified time or time period for determining whether the predetermined condition or conditions are met is often very short, sometimes hours or even minutes.

Binary options typically exercise automatically; once the contract or instrument is entered into, there is no decision for either the buyer or the seller to make. The buyer either

- is entitled to receive a fixed amount if the predetermined condition is met, i.e., the buyer is “in-the-money”, or
- loses all or nearly all of the amount paid if the predetermined condition is not met, i.e., the buyer is “out-of-the-money”.

The yes/no proposition is structured on the performance of an underlying interest. For the purposes of the Instrument, we interpret “underlying interest” as the event or thing that the value or payment obligations of the binary option is based on, derived from or referenced to. The underlying interest of a binary option could be the

- occurrence of a specified event, e.g., the outcome of an election or a change in a benchmark interest rate, or
- performance or value of a security, index, currency, precious metal or any other commodity, price, rate, benchmark, variable or any other thing.

For example, a binary option may be based on a yes/no proposition such as whether:

- the value of the Canadian dollar will be above \$0.75 US on a particular day;
- the price of a share in ABC Company will be above \$14.37 at any time between two particular dates;
- the price of gold will be below \$1082 at 3:42 pm on a particular day;
- the price of oil will be in the range of \$48.00 – \$49.99 at any time on a particular day; or
- there will be more than one inch of rain reported at a specified location on a specific day.

A binary option typically does not grant the buyer or seller any right or obligation to buy, sell, receive or deliver an underlying interest referenced in the contract or instrument. For example, if the yes/no proposition of a binary option is based on the value of a share price, the binary option would provide for settlement in cash and would not provide for delivery of the underlying share. Similarly, if the yes/no proposition of a binary option is based on the movement in the price of gold, the binary option would provide for settlement in cash and would not provide for delivery of physical gold.

Typically, the only rights under a binary option for the buyer or seller are an entitlement to receive or an obligation to pay (a) a fixed amount if the predetermined condition or conditions are met, and (b) a lesser amount or zero if the predetermined condition or conditions are not met. The payout structure of a binary option is non-linear; that is, the payout possibilities are discrete amounts that are specified at the time the contract or instrument is entered into (although the actual value of the payout amount may not be determined at the time the contract or instrument is entered into).

However the product is named, the prohibition in the Instrument applies if the product meets the definition of “binary option” and the specified time for determining whether the predetermined condition is met is less than 30 days from the date the contract or instrument is entered into.

Section 2 – Trading binary options with an individual prohibited

Section 2 prohibits advertising, offering or selling a binary option to an individual. Advertising, offering and selling are elements of “trade” or “trading”. The phrase “or otherwise trade” includes soliciting and all other elements of “trade” or “trading”, including an act in furtherance of a trade.

Section 3 – Trading binary options with a person or company other than an individual prohibited

Section 3 prohibits advertising, offering or selling a binary option to a person or company, other than an individual, that is created, or is primarily used, to trade a binary option. Section 3 is designed to support the prohibition in section 2, by preventing a party that offers a binary option from avoiding the prohibition by having their proposed client create a corporation or other type of entity to trade binary options.

Section 4 – Binary options of 30 days or longer

Section 4 carves out from the prohibitions in sections 2 and 3 a binary option for which the specified time period for determining whether the predetermined condition or conditions are met is 30 days or more from the date the binary option is entered into.

We remind market participants that binary options that are not subject to the Instrument are derivatives and/or securities in each jurisdiction of Canada. Any person or company advertising, offering, selling or otherwise trading such products to persons or companies in Canada is subject to securities legislation in Canada including, for example, anti-fraud provisions and requirements respecting registration, market conduct and disclosure. Furthermore, in jurisdictions of Canada where binary options are regulated as securities, trading a binary option may be a distribution subject to the prospectus requirement.

In Québec, under the qualification regime, any person that wishes to create or market a derivative is required to apply to the Autorité des marchés financiers for qualification before the derivative is offered to the public. A qualified person may only market derivatives that have been

duly authorized by the Autorité des marchés financiers as listed in its qualification decision or in a specific decision following an application by the qualified person. In addition, the qualified person must offer derivatives to the public through a registered dealer, or register with the Autorité des marchés financiers as a dealer.

Offering investment services or products to persons or companies in Canada, whether by telephone, online or in-person, is a regulated activity. Investing through unregistered offshore platforms or dealers can be risky and is a common red flag for investment fraud. The CSA encourage all investors to visit aretheyregistered.ca to check the registration of any person or company 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.

ANNEX C

LOCAL MATTERS

There are no local matters to consider at this time.



INVESTMENT INDUSTRY ASSOCIATION OF CANADA

ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

1 Place Ville-Marie | Bureau 2901
Montréal (Québec) | H3B 0E9514.843.8950 | www.accvm.cawww.accvm.ca

May 25, 2017

Delivery Via Email: consultation-en-cours@lautorite.qc.ca; comments@osc.gov.on.ca

Alberta Securities Commission
Autorité des Marchés Financiers
Financial and Consumer Services Commission (New Brunswick)
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Nova Scotia Securities Commission
Nunavut Securities Office
Ontario Securities Commission
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

Me Anne-Marie Beaudoin
Corporate Secretary
Autorité des Marchés Financiers
800, rue du Square-Victoria, 22e étage
C.P. 246, tour de la Bourse
Montréal, Québec H4Z 1G3

Grace Knakowski
Secretary
Ontario Securities Commission
20 Queen Street West, 22nd floor
Toronto, Ontario M5H 3S8

Re: Proposed National Instrument 91-102 “Prohibition of Binary Options” and Related Proposed Companion Policy (the “Proposed Rules”)

The Investment Industry Association of Canada (IIAC) would like to submit its comments regarding the Proposed Rules on binary options trading.

The IIAC and its Mandate

The IIAC is the national association representing the position of 130 IIROC-regulated Dealer Member firms on securities regulation, public policy and industry issues. We work to foster a vibrant, prosperous investment industry driven by strong and efficient capital markets.

Current Issue

There is currently an issue concerning binary options trading. It is important for the Canadian Securities Administrators (“CSA”) to consider this matter.

Certain investors currently trade binary options on illegal electronic platforms, operated by individuals who have not been approved by regulatory organizations and who have not obtained prior authorization to trade those derivative products. The publication of warning notices by regulatory organizations is evidence of the seriousness of this issue, but regulators, despite their best efforts, seem to be unsuccessful in putting an end to the problem.

As will be mentioned below, we believe that this trading activity to retail investors must be regulated by Canadian regulators to ensure the protection of the public against unfair, abusive and fraudulent practices, including the risk of diversion of funds outside of Canada. We believe that brokers regulated by the Investment Industry Regulatory Organization of Canada (“IIROC”) should be allowed to offer binary options to retail investors to prevent these individuals from fraudulent trading.

In addition, certain investors mistake the current unlawful activity for that of regulated brokers in Canada. The reputation of our industry is, therefore, indirectly at stake.

Legal trading vs. Fraud

It should be stressed that there are two types of “trading” currently occurring in Canada:

1. Institutional and sophisticated investors trading binary options legally;
2. Investors using fraudulent online platforms to be scammed out of their money.

We believe the proposed rules could potentially disrupt “legal” binary options trading currently executed by our members without preventing the “scamming” performed by fraudsters.

Legal trading: Binary Options and Their Use in our Industry

Binary options are not the problem, per se. Their structure, as well as their mechanism, is simple.

Binary options are often referred to as digital or all-or-nothing options. Binary options can also be listed on renowned markets such as the Chicago Board Options Exchange. Institutional and sophisticated investors (including closely held corporations) use them in order to increase the returns on their investments while taking on the risks involved. The issue we are currently facing is not related to binary options per se, but is a problem of another nature.

Illegal trading: Illegal Platforms and Fraudsters

As mentioned above, the industry's concerns are not on the structure of binary options, but rather on the way in which they are offered to investors by fraudsters. The issue lies with the offers made illegally by individuals who are not registered and not authorized under applicable laws. No issues lie with the "legal" binary options trading executed by institutional or sophisticated investors.

Illegal online trading sites (often based abroad) provide incorrect information to investors and indicate that there is no risk involved in the transactions performed on their electronic platforms. The fraudsters behind these platforms manipulate the price of the underlying securities in order to "win" against the investor. In certain cases, investors could "win," but they will rarely receive the profit earned. In the latter case, the counterparty risk is related to the settlement of the product by fraudsters. The fact that there is no central clearing poses a major risk of fraud for individuals. The increase in the number of complaints made by clients who have lost their capital is evidence of this problem.

In addition, these trading sites are not registered with regulatory organizations and the individuals operating them are not registered as derivatives brokers or members of a self-regulating body and of an investor protection fund. Considering the illegality of these activities with derivatives in Canada, not to mention the risk of unfair, abusive or fraudulent practices for the investing public, it is essential for the CSA to ensure the enforcement of its regulations on derivatives by specific measures aimed at suppressing these violations. Certain fraudulent operation sites even indicate, incorrectly, that they are registered with regulatory organizations. These websites must be shut down.

We further believe that the RCMP must be involved in stopping these international fraudsters. The RCMP should shut down these sites and try to prosecute these criminals with the help of international law enforcement agencies.

Proposed Rules and their Impact

We see certain issues with the Proposed Rules. For example, the definition of a “binary option” in the Proposed Rules should be amended as it currently covers legitimate binary option transactions executed by institutional and sophisticated investors.

More importantly, since these electronic trading platforms are operated by fraudsters, we doubt they would chose to comply with the Proposed Rules if they were implemented. Therefore, the Proposed Rules will not end the illegal activity and may interfere with the current “legal” institutional binary options trading taking place in the Canadian market.

We also note that Section 3 proposes to prohibit retail investors from circumventing a trading ban by establishing a company or trust for the purpose of trading binary options. We believe that any retail investor that will have the means to create a company or a trust in order to circumvent a trading ban should be considered a sophisticated investor. No protection would be needed for this type of individual. We therefore believe that Section 3 of the Proposed Rules should be removed.

Binary Options Transactions through Regulated Firms

In order to end illegal transactions, regulatory organizations must consider the possibility of allowing IIROC-regulated brokerage firms to be registered to offer these products to all investors. Furthermore, regulators must correctly define binary options to avoid confusion in the industry.

Dealing with an IIROC-regulated firm will allow investors who wish to trade binary options to properly understand the product as well as the significant risks involved. Furthermore, there would be no risk of fraud in regulated and legal trading as is present on illegal trading platforms.

We also believe that since our members are IIROC-regulated brokers, they should be exempt from the application of the Proposed Rules if they can offer binary options to retail investors.

IIROC and the CSA: Informing the Investor

As it is IIROC’s mission to protect the investor, legal and regulated binary options trading will be beneficial to experienced investors seeking this kind of product. The IIROC strict regulatory framework would allow clients to gain an understanding of this kind of product through disclosure obligations before a transaction is executed. In addition, clients of full-service firms will be protected by the concept of investment suitability.

We also believe that it is essential for the CSA to keep informing the investing public about the fraud occurring on illegal trading platforms in order to stop the criminals. The CSA must also warn investors about the “Scammed by binary options? We help recover your money” scam created by these criminals.

Conclusion

The IIAC and its members urge the CSA to prevent illegal binary options trading in order to protect investors and contribute to the integrity of our industry. We believe this must be done by allowing IIROC-regulated brokers to offer binary options and not through the Proposed Rules. As previously mentioned, we highly doubt that the criminals would comply with these rules.

As mentioned above, binary options are not the problem. The fraudulent and illegal trading of this product is the issue and must be stopped.

Regulatory bodies must consider the possibility of registering certain regulated firms to trade this product legally, with no risk of fraud, and with a strict regulatory framework to protect Canadian investors.

We believe investor education and warnings must continue in order to stop the illegal and fraudulent binary option activity in Canada. The only way to prevent online fraud is the tell Canadians about this “trading” scam as well as the related “we help recover your money” scam.

Furthermore, we believe that international law enforcement agencies must work together to stop these criminals.

Please note that the IIAC and its Members, as always, remain available for further consultations.

Yours sincerely,



Annie Sinigagliese
Managing Director
Investment Industry Association of Canada
asinigagliese@iiac.ca



Canadian Market
Infrastructure Committee

Via e-mail to: consultation-en-cours@lautorite.gc.ca
comments@osc.gov.on.ca

Alberta Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Nova Scotia Securities Commission
Nunavut Securities Office
Ontario Securities Commission
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

May 29, 2017

Dear Sirs/Mesdames:

Re: Proposed National Instrument 91-102 *Prohibition of Binary Options* (“NI 91-102”) and Related Proposed Companion Policy (the “Companion Policy”, and together with NI 91-102, the “Proposed Rules”)

INTRODUCTION

CMIC is pleased to provide this comment letter on the Proposed Rule.

CMIC was established in 2010, in response to a request from Canadian public authorities,¹ to represent the consolidated views of certain Canadian market participants on proposed regulatory and legislative changes in relation to over-the-counter (“**OTC**”) derivatives. The members of CMIC who are responsible for this letter are: Alberta Investment Management Corporation, Bank of America Merrill Lynch, Bank of Montreal, Caisse de dépôt et placement du Québec, Canada Pension Plan Investment Board, Canadian Imperial Bank of Commerce, Citigroup Global Markets Inc., Deutsche Bank A.G., Canada Branch, Fédération des Caisses Desjardins du Québec, Healthcare of Ontario Pension Plan Trust Fund, HSBC Bank Canada, Invesco Canada Ltd., Manulife Financial Corporation, Morgan Stanley, National Bank of Canada, OMERS Administration Corporation, Ontario Teachers’ Pension Plan Board, Royal Bank of Canada, Sun Life Financial, The Bank of Nova Scotia and The Toronto-Dominion Bank.

CMIC brings a unique voice to the dialogue regarding the appropriate framework for regulating the Canadian OTC derivatives market. The membership of CMIC has been intentionally designed to

¹ “Canadian public authorities” means representatives from Bank of Canada, Canadian Securities Administrators, Department of Finance and The Office of the Superintendent of Financial Institutions.

present the views of both the 'buy' side and the 'sell' side of the Canadian OTC derivatives market, including, but not limited to, both domestic and foreign owned banks operating in Canada as well as major Canadian institutional market participants (including a number of major pension funds) in the Canadian derivatives market. This letter reflects the consensus of views within CMIC's membership about the proper Canadian regulatory and legislative regime applicable to the OTC derivatives market.

In this letter, we will address concerns that we have with respect to the Proposed Rules. Mainly, CMIC members are concerned that the proposed prohibition of trading binary options could disrupt their legitimate binary option business.

POLICY CONCERNS AND GENERAL EXCEPTION

Based on the CSA Notice and Request for Comments (the "**Notice**") accompanying the Proposed Rules, the CSA are concerned by the number of complaints received in connection with online binary options platforms. We understand that these electronic trading platforms are operating illegally in Canada and, in many cases, are acting fraudulently. Warning notices about this activity have been published by regulators indicating the severity of this issue. However, CMIC submits that, in all likelihood, the Proposed Rules will not effectively stop this illegal activity in Canada while, at the same time, have the unintended effect of interfering² with current, legitimate binary option business of certain members of CMIC.

It is CMIC's view that the transactions entered into on these online binary option platforms are gambling transactions disguised as financial transactions. Participants must pay to play, money is transferred offshore where it remains and there is no secondary market for these transactions. These platforms target individuals, promising quick returns by "predicting" the outcome of a scenario. In fact, the mis-labelling and fraudulent marketing of these products as "Binary Options" by the individuals behind these platforms is itself part of the deception to create legitimacy. Given that legalized gambling exists only under the authority of the Criminal Code, and these types of online binary option platforms do not appear to comply with the requirements of the Criminal Code, we submit that this activity should be regulated by the applicable gambling authority in each province.³ Further, if these platforms have indeed been identified as vehicles to commit fraud, CMIC submits that the Commercial Crime Branch of the RCMP should handle investigations and prosecution of these platforms. The regulation of these platforms does not seem to appropriately fall under the jurisdiction of the CSA. It should be noted that a similar approach is taken in the UK where binary options are not regulated by the Financial Conduct Authority, however, firms dealing in in binary options with remote gambling equipment located in Great Britain need to be regulated by the Gambling Commission.⁴ Further, the Financial Industry Regulatory Authority in the U.S. does not regulate binary option activity but instead warns consumers about the risks of dealing with binary options and explains how consumers may be scammed.⁵

While we believe that online binary option platform activity should be regulated as a gambling matter, as opposed to a securities or derivatives matter, we will provide comments on the specific questions set out in the Proposed Rules.

² See discussion under "Definition of Binary Options", "Prohibition to Sell to Individuals" and "Attempt to Prohibit Work-Around of Trading Ban" sections for an explanation of this interference.

³ For example, in Ontario, the Ontario Lottery and Gaming Corporation.

⁴ See: <https://www.fca.org.uk/consumers/binary-options-uk>.

⁵ See: <http://www.finra.org/newsroom/2017/binary-options-follow-schemes-dont-lose-money-twice>.

However, if the CSA takes the position that the issuance of the Proposed Rules is necessary, the Proposed Rules should provide for a general exception if the binary option is being sold by a registered derivatives dealer, or by a derivatives dealer exempt from registration (in either case, a “**Derivatives Dealer**”).

BINARY OPTIONS SOLD TO SOPHISTICATED INDIVIDUALS

It is CMIC’s view that prohibiting binary options specifically is too prescriptive of a rule as online platforms can easily offer another type of option or derivatives generally to individuals as a money-making scheme. The more important aspect of the Proposed Rules is to whom binary options are being marketed and sold.

The Proposed Rules prohibit advertising or trading a binary option to or with an individual. While it is important to protect individuals, CMIC submits that only an unsophisticated individual is in need of such protection. Sophisticated individuals have the ability to analyze and discern the risks inherent in binary option transactions. From a policy perspective, this concept is, of course, not new. For example, an individual who, either alone or together with a spouse, has net assets of at least \$5 million is considered an “accredited investor” and thus is considered sufficiently sophisticated that securities can be sold to them without a disclosure document.

Currently, barrier options are being sold by certain CMIC members to sophisticated individuals, many of whom trade through closely-held corporations. If the Proposed Rules were in effect, this trading activity would be prohibited, thus interfering with current, legitimate, binary option business of certain members of CMIC. Barrier options are tools that are currently being used by sophisticated individuals (including through closely-held corporations) and are not uncommon in the foreign exchange market. Accordingly, CMIC submits that trading barrier options with sophisticated individuals should not be prohibited under the Proposed Rules in order for this trading to continue while at the same time, enabling regulators to satisfy their policy objectives.

DEFINITION OF BINARY OPTIONS

The definition of a “binary option” in the Proposed Rules is, in CMIC’s view, too broad and covers binary transactions currently being entered into legitimately by some members of CMIC. For example, the ISDA 2005 Barrier Option Supplement to the 1998 FX and Currency Option Definitions (the “**Barrier Option Supplement**”)⁶ describes multiple types⁷ of binary option transactions which are commonly entered into.

In order to avoid capturing legitimate barrier option transactions under the Proposed Rules, CMIC submits that the Proposed Rules should clarify that transactions subject to the Barrier Option Supplement and governed by an agreement which evidences the legitimate trading relationship between the parties are excluded from the definition of “binary option”.

⁶ Available here: <https://www.newyorkfed.org/medialibrary/microsites/fxc/files/2005/fxc051206a.pdf>.

⁷ For example, two popular types of barrier option transactions are a “One-Touch” option and a “Double No-Touch” option. Under a “One-Touch” option, a payout occurs once the price of the underlying asset reaches or surpasses a predetermined barrier. Only two outcomes are possible: the barrier is breached and the counterparty collects the full payout agreed, or the barrier is not breached and the counterparty loses the full premium. The “Double No-Touch” option provides for an agreed upon payout if the price of the underlying asset does not reach or surpass one of two predetermined barrier levels. If the price of the underlying asset does not remain within range of the two barriers, the counterparty loses the full premium.

In addition, it is CMIC's view that (i) the words, "a lesser amount or" should be deleted from section 1(b) of NI 91-102, and (ii) only transactions that are "derivatives" under the *Derivatives: Product Determination* rules⁸ should be considered "binary options" under the Proposed Rules. These proposed changes would assist in alleviating the risk that other products, including those that do not involve an "all or nothing" approach, would be captured under this definition.

While, in CMIC's view, the above recommendations may not capture all transactions being entered into legitimately by certain CMIC members, it will capture a majority of them.

ATTEMPT TO PROHIBIT WORK-AROUND OF TRADING BAN

Section 3 of the Proposed Rules attempts to prohibit individuals from working around the trading ban by establishing a company or a trust to enter into binary options. In CMIC's view, this provision is not appropriate and should be deleted.

From a practical perspective, if this provision were implemented, every Derivatives Dealer will need to look behind its counterparty to determine whether it was established or is primarily used to trade a binary option for an individual. Given the broad wording of the provision ("...a person or company that is not an individual"), this means the determination needs to be made in respect of all or almost all of the counterparties of a Derivatives Dealer. In CMIC's view this approach is not practical and, as discussed below, unnecessary.

Also, in CMIC's view, section 3 of the Proposed Rules is unnecessary as any individual who has the ability to set up a company or a trust in order to work around this trading ban is, *de facto*, a sophisticated individual. Such individual should not need the protection of the Proposed Rules. Accordingly, CMIC recommends that section 3 of the Proposed Rule be removed.

TERM OF BINARY OPTION (30 DAYS)

Section 4 of the Proposed Rules provide that the trading ban under section 2 does not apply to binary options with a term greater than 30 days. In CMIC's view, the 30 day term appears arbitrary. We recommend that the regulators review all product offerings of online binary option platforms to determine the normal term of binary options offered and from that, recommend an appropriate term. Further, it is CMIC's view that guidance should be provided that even if the term of the transaction is greater than the 30 days (or the appropriate term once the recommended research is performed), a transaction would not be caught by the prohibitions of the Proposed Rule if the barrier event occurs within the first 30 days (or such appropriate term).⁹

PROPOSED RULE DOES NOT ACCOMPLISH INTENDED PURPOSE

The Notice asks for commentary as to whether the Proposed Rules will accomplish the intended purpose. CMIC respectfully submits that the Proposed Rules do not accomplish the intended purpose.

The motivation behind the Proposed Rules is to protect would-be investors from becoming victims of binary options fraud and from becoming victims of an illegal promotion of an extremely high risk product. In CMIC's view, the fraudsters that are operating these online binary option platforms are unlikely to comply with the Proposed Rules and the only effective means of influencing these

⁸ OSC Rule 91-506, MSC Rule 91-506, AMF Regulation 91-506 and Multilateral Instrument 91-101.

⁹ For example, a binary option transaction could have a term of one year, but with barrier type of events that occur within the first 30 days, such as a cancellation event that is in the counterparty's favour with a zero amount being paid.

platforms is through enforcement actions. CMIC submits that the market participants that will comply with the Proposed Rules, such as the 'sell' side members of CMIC, are already complying with all applicable securities laws and regulations. Unfortunately, those counterparties are not the ones with whom the CSA membership is concerned in connection with binary options and, accordingly, CMIC does not believe that the implementation of the Proposed Rules will stop the online binary options platform fraudsters from preying on investors that are individuals.

In CMIC's view, a better and more effective approach would be to (i) treat these transactions as gambling transactions subject to the Criminal Code and enforcement by the RCMP, and (ii) raise awareness among investors by continuing to conduct an investor educational program, such as creating websites such as www.binaryoptionsfraud.ca, holding investor information seminars and taking out newspaper and television advertising warning of the dangers of buying binary options from online platforms.

CMIC welcomes the opportunity to discuss this response with you. The views expressed in this letter are the views of the following members of CMIC:

Alberta Investment Management Corporation
Bank of America Merrill Lynch
Bank of Montreal
Caisse de dépôt et placement du Québec
Canada Pension Plan Investment Board
Canadian Imperial Bank of Commerce
Citigroup Global Markets Inc.
Deutsche Bank A.G., Canada Branch
Fédération des Caisses Desjardins du Québec
Healthcare of Ontario Pension Plan Trust Fund
HSBC Bank Canada
Invesco Canada Ltd.
Manulife Financial Corporation
Morgan Stanley
National Bank of Canada
OMERS Administration Corporation
Ontario Teachers' Pension Plan Board
Royal Bank of Canada
Sun Life Financial
The Bank of Nova Scotia
The Toronto-Dominion Bank



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BY COURIER AND EMAIL

May 29, 2017

Alberta Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Nova Scotia Securities Commission
Nunavut Securities Office
Ontario Securities Commission
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

Attention: Me Anne-Marie Beaudoin
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Toronto, Ontario M5H 3S8
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Dear Ms. Beaudoin and Ms. Knakowski:

Re: Proposed National Instrument 91-102: *Prohibition of Binary Options and Related Proposed Companion Policy*

The North American Derivatives Exchange, Inc. ("Nadex") is pleased to provide this comment letter to the Participating Jurisdictions with respect to their Proposed National Instrument 91-102 *Prohibition of Binary Options* ("Instrument") and Proposed Companion Policy 91-102 *Prohibition of Binary Options* ("CP") (collectively, the "Proposed Instrument").

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Nadex is registered with the United States Commodity Futures Trading Commission (“CFTC”) both as a Designated Contract Market (“DCM”) and a Derivatives Clearing Organization (“DCO”). Nadex is one of several U.S. exchanges that list binary options for trading by retail traders. Nadex offers binary options on the widest variety of asset classes of all these exchanges: FX rates, stock index futures, commodities, agricultural futures and economic events. Other US exchanges listing binary options for retail traders include NYSE MKT (single-stock “Binary Return Derivatives”), CBOE (binary options on the S&P 500 Cash Index and the VIX Index) and Cantor Exchange (binary options on FX rates, spot gold and silver and various weather events). Nadex and Cantor Exchange are CFTC-regulated, while NYSE MKT and CBOE are regulated by the United States Securities Exchange Commission. These exchange listed binary options have durations ranging from weekly expirations to daily and intraday expirations. As discussed in more detail below, however, the binary options that Nadex and these other US exchanges list are markedly different than the types of “binary options” that Nadex believes are the driving force behind the Proposed Instrument.

As a regulated market, Nadex wholeheartedly supports the Participating Jurisdictions’ stated purpose in putting forward the Proposed Instrument “to help protect would-be investors from binary options fraud”. However, we believe the Proposed Instrument goes too far in focusing on a particular product as opposed to the bad actors in the space and in broadly defining the product to include the types of perfectly legitimate financial instruments traded on Nadex and other US exchanges. Moreover, the proposal fails to differentiate between the simple up/down contracts marketed predominantly by entirely unregulated firms and labelled as “binary options” (“**fifty/fifties**”), and the genuine volatility-driven 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 (“**volatility binaries**”). We understand that the vast majority, if not all, of consumer complaints generated in connection with the marketing and sale of “binary options” concern the fifty/fifties, not the marketing, sale and trading of volatility binaries.

BENEFITS OF BINARY OPTIONS

With regard to investment needs, volatility binaries allow retail clients to access market risk simply, cheaply and conveniently. This risk may be purchased to offset an existing risk on a wider investment portfolio or economic exposure (i.e. to hedge) or it may be purchased to establish a standalone speculative position.

We do not believe that the discrete nature of binary contract pay-outs, and the fact that these pay-outs do not match perfectly against the continuous returns generated by an investment portfolio, mean they cannot have a role in hedging such investment portfolios. Most hedges are not perfect and there is utility in establishing a partial hedge; the mismatch in pay-outs between a binary pay-out and the loss on an investment portfolio will be compensated for, in the opinion of many investors, by the fact that the loss on a binary hedge (in the event of good performance in their underlying investment portfolio) is also capped.

Volatility binaries (but not fifty/fifties) are the only instrument that could be available to retail clients who want to hedge or speculate on market volatility in a controlled, limited risk manner. No other product commonly available to retail clients can deliver both a bullish and bearish exposure to volatility with a strict cap on risk in either case.

Volatility binaries (but not fifty/fifties) are also the only instrument that could be available to retail clients who want to hedge against, or speculate on, very short term market volatility, for instance of the type created by the release of specific major economic figures. The short tenors available on these instruments allows retail clients a clean exposure to the volatility potentially created by the scheduled release of economic news. Conventional “vanilla” call and put options typically have tenors stretching over days, weeks or months, creating a blended exposure to a broad range of volatility-based risks, not all of which may be of concern or interest to a particular retail client.

Finally, we believe volatility binaries are intuitively well understood, and are traded with great satisfaction, by retail traders. The price of a volatility binary represents the percentage likelihood of a particular market event occurring; for example, the market is indicating that a binary option trading at a best bid of 60 and a best offer of 64 has a 62% (the midpoint of the best bid-ask) likelihood of finishing in the money. This is a proposition that retail traders understand well and on which they are able to form their own independent view.¹

BENEFITS OF NADEX’S BUSINESS MODEL

In addition to the inherent benefits of binary options discussed above, we believe Nadex’s business model offers further benefits to retail traders in the binary options space. As an exchange and clearinghouse, Nadex can offer retail traders all the traditional benefits of formal, regulated markets, including security of funds held by a regulated clearinghouse, rules that govern the fair operation of the market, oversight by a federal regulator, transparent central limit order books, liquidity to enter and exit a position, etc. At the same time, we offer retail traders products designed them, not for large institutions. So, an individual trader on Nadex can trade \$100 contracts – much smaller size than the futures contracts and options typically offered on exchanges – and Nadex’s contracts have absolutely capped risk (and potential reward). All contracts traded on Nadex are fully collateralized with the maximum risk funded up front. As a result, the trader knows his or her full risk at the time they place a trade and even if the underlying market moves strongly against them, they may lose that initial investment but they will never receive a margin call for additional funds to cover losses on that position in excess of their initial investment. In short, Nadex provides a market that offers products designed for retail traders, listed on a regulated exchange.

¹ Unlike the straightforward volatility binaries, fifty/fifties are typically priced as a wagered amount that pays out some percentage of that wagered amount, e.g., 85%, if the contract finishes in the money, and may pay out a small “consolation amount”, e.g., 10%, in the event the contract finishes out of the money. This pricing model tends to obscure the cost of the fifty/fifties to the trader.

SPECIFIC QUESTIONS:

1. Does the proposed definition of “binary option” capture contracts or instruments that should not be captured? If so, please specify the types of contracts or instruments that should not be captured and on what basis they would be captured.

We believe the Participating Jurisdictions should apply two distinct regulatory approaches to what are, in effect, two distinct products:

1. Fifty/Fifties of the type typically marketed to Canadian consumers by incoming online platforms that are lightly regulated, or entirely unregulated; and,
2. Conventional, volatility-based binary options of the type offered to retail traders by Nadex and other US exchanges and by some regulated OTC firms in Europe, Japan and elsewhere.

We think the fifty/fifty binaries have commonly become identified with the term “binary option” but these should best be considered not as an option but as a financial instrument with the economic characteristics of a fixed odds bet. In this regard, we agree that these fifty/fifties have been widely mis-sold to unsophisticated consumers throughout Canada and elsewhere by unregulated firms with very significant negative consumer outcomes as a result. We support any steps the Participating Jurisdictions make in addressing this unsatisfactory situation. Indeed, we think that the scale of the mis-selling is so great it may be appropriate to refrain from permitting regulated firms in Canada from offering the fifty/fifties contract type; i.e., continue the current ban on such contracts in Canada.

We believe, however, that genuine binary options – volatility binaries – have not been mis-sold, are not particularly susceptible to mis-selling and meet a clear investment need for clients who want to hedge, or speculate on, market volatility in a controlled, limited risk manner. They are widely available to retail audiences in other well-regulated markets, such as the US and Japan, and are sufficiently different to the fifty/fifties that a separate regulatory approach is appropriate. That is, the offering of volatility binaries, like vanilla put and call options or other legitimate financial instruments, should be permitted as long as the offeror is appropriately regulated and applicable requirements (client onboarding, risk disclosure, transparency, etc.) are otherwise met.

2. The Proposed Instrument applies to binary options where the time period specified in the binary option for determining whether the predetermined condition or conditions are met is less than 30 days from the date the binary option is entered into. Is this time period appropriate? Please specify why or why not.

We do not believe that short durations in and of themselves prevent investors from making informed decisions, or necessarily transform a trading product into something inappropriate. Indeed, all contracts that are available for trading on an exchange have a fixed duration and, no matter its initial term, even a longer term contract will eventually become a one-

day, then a one-hour, then a 1-minute contract as it nears expiration. We believe a 30-day limit is arbitrary. Moreover, it appears that such a 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.

3. Staff considered a variety of options that would prevent circumvention of the binary options trading ban. These included provisions that would capture indirect trading by an individual through a company, trust or other entity. As currently drafted, the Proposed Instrument includes an anti-avoidance provision that would ban trading binary options with a person or company that is created, or primarily used, to trade binary options. We believe this approach captures our intent to prohibit attempted work-arounds of the binary options trading ban without increasing the complexity of the rule. Is the proposed provision unambiguous and clear, or should the scope of this provision be modified, for example, to more specifically extend to any person, company or other entity wholly-owned or controlled by an individual?

As discussed below, Nadex does not believe efforts to designate a particular product as "illegal" or to carve out trading by certain types of market participants (entity v. individual) ultimately will be successful in achieving the Participating Jurisdictions' objectives. To the contrary, only actions that attack the parties that are acting inappropriately – the unregistered purveyors of on-line binary options – and that limit demand for the illegal product – for example, allowing registered firms and exchanges to offer legitimate volatility binaries as a quality alternative to the unregulated fifty/fifties – will ultimately reduce the amount of fraud currently occurring in the area.

4. Do you believe the Proposed Instrument will accomplish the intended purpose of proposing it, as set out in this Notice?

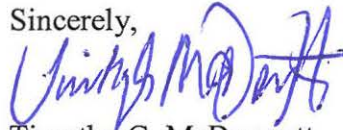
As the Participating Jurisdictions note, the "binary options" that currently are being marketed in Canada already are illegal offerings. We do not believe that the Proposed Instrument will cause those currently illegally offering those products to stop. The better approach, we believe, is to allow regulated firms and/or exchanges to offer volatility binaries as an alternative to the fifty/fifties being marketed in Canada by unregulated firms. This will provide a quality, legal alternative to meet a clear investor interest. At the same time, we believe efforts to attack the bad actors rather than the financial instrument will more effectively protect the Canadian public. For example, Visa and MasterCard recently have taken steps – presumably with the encouragement of the Participating Jurisdictions – to limit the availability of funding to unregistered purveyors of binary options.² The Participating Jurisdictions could also work with Google, Yahoo and

² See *Visa Tightens Screws on Binary Options, Targeting US and Canada* (Sept. 26, 2016), <http://www.financemagnates.com/binary-options/regulation/exclusive-visa-tightens-screws-on-binary-options-targeting-us-and-canada/>, and *MasterCard Determined to Cut Binary Options Deposits from Canada* (Nov. 21, 2016), <http://www.financemagnates.com/binary->

other search engine providers to limit on-line advertising of illegal services to Canadian consumers. We believe such efforts, in concert with enforcement actions taken by the Participating Jurisdictions against the unregulated purveyors of fifty/fifties, will be much more effective in protecting consumers than attempting to ban a financial product.

Thank you for considering our comments. Please contact the undersigned at +1-312-884-0171 or tim.mcdermott@nadex.com if you have any questions about our comments or you would like to meet with us to discuss them further.

Sincerely,



Timothy G. McDermott

Chief Executive Officer

North American Derivatives Exchange, Inc.

[options/regulation/exclusive-mastercard-determined-to-cut-binary-options-deposits-from-canada/](#).



May 29, 2017

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Ontario Securities Commission
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

Attention to:

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Dear Sirs/Mesdames:

RE: Proposed National Instrument 91-102 *Prohibition of Binary Options* and Related Proposed Companion Policy

Bourse de Montréal Inc. (the "Bourse") and the Canadian Derivatives Clearing Corporation ("CDCC") appreciate the opportunity to comment on National Instrument 91-102 *Prohibition of Binary Options* and its Proposed Companion Policy 91-102 *Prohibition of Binary Options* (collectively, the "Proposed Instrument") proposed by the securities regulatory authorities in all Canadian jurisdictions other than British Columbia (collectively, the "Participating Jurisdictions"). The Bourse and CDCC fully support the

Participating Jurisdictions' policy objectives of protecting Canadian investors and generally strengthening the integrity of, and public confidence in, the financial sector. We respectfully submit that these policy objectives can be met by narrowing the scope of the proposed prohibition such that the offering of products that are traded on a recognized exchange or cleared by a recognized clearing house, would not be prohibited. Our rationale is provided below.

The Bourse and CDCC

The Bourse is a derivatives exchange recognized by the Autorité des marchés financiers ("AMF") and exempted from recognition by the Ontario Securities Commission (the "OSC") and CDCC is a clearing house recognized by the AMF, the OSC and the British Columbia Securities Commission (collectively and respectively for each of the Bourse and CDCC, the "Regulating Commissions"). The Bourse and CDCC are part of the TMX Group organization, the key subsidiaries of which operate cash and derivative markets for multiple asset classes including equities, fixed income and energy. The Bourse, CDCC, Toronto Stock Exchange, TSX Venture Exchange, Alpha Exchange, The Canadian Depository for Securities, Natural Gas Exchange, Boston Options Exchange, Shorcan, Shorcan Energy Brokers and other TMX Group companies provide listing markets, trading markets, clearing facilities, data products and other services to the global financial community.

Policy Objective and Scope of the Proposed Instrument

The Participating Jurisdictions' stated concern that forms the basis for the Proposed Instrument is that products commonly referred to as binary options are being offered illegally to retail customers in Canada via unauthorized on-line trading platforms. Through the Proposed Instrument, Participating Jurisdictions aim at protecting "would-be investors from becoming victims of binary options fraud and from becoming victims of an illegal promotion of an extremely high risk product, by raising awareness among investors that these products are illegal and by disrupting the advertising and facilitation of these products." To this end, the Proposed Instrument would explicitly prohibit advertising, offering, selling or otherwise trading a binary option to an individual.

The Bourse and CDCC support the Participating Jurisdictions' efforts to protect investors by ensuring that products cannot be sold to investors through unauthorized mechanisms. However, as currently drafted, the Proposed Instrument is so broad in scope that it may have the effect of prohibiting the offering to an individual of an instrument otherwise duly listed or cleared by the Bourse or CDCC. It is unclear what the justification might be for this type of products to warrant an across-the-board prohibition rather than falling under the detailed regulatory oversight regimes applicable in each Participating Jurisdiction that has proven effective with respect to other types of instruments. Any financial product, and not only binary options, that is offered illegally to Canadian investors poses a threat to investors' protection.

The respective Regulating Commissions have direct oversight over the Bourse and CDCC. All products that trade on the Bourse must be submitted to the Regulating Commissions as part of the self-certification process established under the Quebec *Derivatives Act* and its regulation and in accordance with the Exemption Order issued on July 27, 2012 by the OSC. Thus, in the event that a binary option or similar

derivative were to be offered for trading on the Bourse, the Regulating Commissions would be in a position to review such product as well as the proposed exchange rules related to such product. As with any other exchange-traded derivatives, the offer of such an instrument to an individual in Canada would be permitted only in accordance with applicable legislation, including dealer registration requirements, of the Participating Jurisdictions. Thus, the relevant Participating Jurisdiction would have complete oversight with respect to the offering of binary options or similar derivatives that are traded on the Bourse.

Under applicable legislation or recognition and exemption orders, before the Bourse is permitted to list a new product, it is required to submit detailed information about such product to the Regulating Commissions. If any of the Regulating Commissions determines that the proposed product is not compliant with relevant legislation, then such Regulating Commission has the option of preventing its launch or requesting amendments to it. Similarly, if CDCC was to act as clearing house for an over-the-counter or exchange-traded binary options or for similar derivatives, it would be permitted to do so only after the proper amendment of its rules, which would have to be reviewed by the Regulating Commissions. Accordingly, if the Bourse had to list binary options, or if CDCC was to clear binary options traded on or off the Bourse, they would do so within the existing regulatory oversight framework. In such a case, the individual to whom an exchange-traded instrument would be offered would benefit from the advantages and protections of trading on an exchange duly recognized in Canada and through a dealer duly registered in Canada. As a consequence, we believe that the Proposed Instrument should be limited to avoid prohibiting the offer by a registered dealer of an instrument traded on a recognized exchange, such as the Bourse, or cleared by a recognized clearing house, such as CDCC.

For the sake of greater clarity and legal certainty, and given the current regulatory oversight framework applicable to the Bourse and CDCC, we believe that the Proposed Instrument should expressly exclude from its application the offer of instruments that are listed on an exchange recognized in Canada or that are cleared centrally by a clearing house recognized in Canada, rather than relying on the ability of certain regulators to grant an exemption from the application of the Proposed Instrument as provided for under Section 5 thereof. It is also important to note that one objective of the Proposed Instrument as stated by the Participating Jurisdiction is to "reduce investor confusion about this form of product by making it clear that binary options are prohibited for individuals." We believe that a clearly spelled-out exemption in the Proposed Instrument for binary options traded on a recognized exchange or cleared by a recognized clearing house, and offered by a duly registered dealer, would reduce investor confusion more effectively than an ad-hoc approach to exemptions as contemplated by the Proposed Instrument.

Definition of Binary Options

The proposed definition of binary option could potentially be over inclusive. For example, the Bourse currently offers "weekly options", which have a life cycle of less than 30 days, and which are used by individual investors. We trust that the Proposed Instrument does not aim at prohibiting the offering of the Bourse's weekly options to individuals, but the proposed definition could potentially be read as including those weekly options and further confuse investors. We reiterate that a clear exemption built into the Proposed Instrument for products traded on a recognized exchanged and/or cleared by a recognized clearing house would alleviate such confusion.

Foreign Precedents

In the United States, regulators have not imposed a complete ban on binary options. In fact, the U.S. Commodity Futures Trading Commission ("CFTC") allows certain designated entities to offer binary options and similar products. For example, the Nadex (North American Derivatives Exchange) can legally offer binary options. Nadex is designated by the CFTC as a Designated Contract Market and a Derivatives Clearing Organization. According to these designations and under the supervision of the CFTC, Nadex is authorized to offer binary options. Nadex's binary options products are traded on seven global indices, ten currency pairs, seven commodities, and three events (rates, unemployment and economic data on job creation). Similarly, the Chicago Board Options Exchange (CBOE) offers binary options on the S&P 500 (BSZ) and VIX (BVZ) indices.

It is also worth noting that the CFTC is actively listing foreign entities that illegally solicit U.S. residents to trade binary options as well as entities that are operating illegally without being registered on its Registration Deficient (RED) List, available at www.SmartCheck.gov/REDList. Such a list helps protect U.S. residents by clearly identifying entities that are acting illegally in the binary options market. Other U.S. regulators and self-regulatory organizations, like the Securities Exchange Commission and the Financial Industry Regulatory Authority (FINRA), also provide information and issue cautionary notices around binary options.

We agree with the approach, taken by U.S. regulators, that does not systematically prohibit all binary options, but rather allows such products to be offered by regulated entities under the supervision of a regulator while actively taking steps to inform U.S. residents and protect them from illegal offerings of binary options and other financial products. We respectfully submit that the Participating Jurisdictions should consider adopting a similar approach. To the extent that these products are deemed appropriate for listing or clearing through the current oversight regime, such products could be traded on a recognized exchange such as the Bourse, cleared by a recognized clearing house such as CDCC and offered to individual investors through registered dealers.

The Bourse and CDCC appreciate the opportunity to provide comments with respect to the Proposed Instrument. We hope that you will consider our suggestions and we would be happy to discuss these at greater length. Please contact the undersigned with any questions you may have.

Yours truly,

(s) Sabia Chicoine

Sabia Chicoine
Chief Legal Officer, MX, CDCC

Martin McGregor

From: Tyson G
Sent: May-25-17 5:59 PM
To: Martin McGregor
Subject: Binary options

Hello Martin

I am a binary option trader. I am quite baffled on how so many people are getting scammed and complaining. Are they not doing research . When I wanted to get into this type of trading I researched everything from brokers to strategys. I also had money to burn if I lost it oh well. That being said I knew this was not get rich quick and I feel so many people think it is . To many people want the results and don't want to put in the hard work of learning and struggling. So then they loose everything and say they got scammed .

The new 30 day min expire time is ridiculous. The president could type one tweet and change the way the usd behaves in a heart beat. If I have to wait 30 days I would be losing. Lazy people need to be educated that this is high risk and not a get rich quick scheme it is day trading at its finest get in get out . Please don't ruin it for the educated investors because of a few novices

Concerned Trader

June 22, 2017

BY EMAIL

Alberta Securities Commission
 Autorité des marchés financiers
 Financial and Consumer Services Commission (New Brunswick)
 Financial and Consumer Affairs Authority of Saskatchewan
 Manitoba Securities Commission
 Nova Scotia Securities Commission
 Nunavut Securities Office
 Ontario Securities Commission
 Office of the Superintendent of Securities, Newfoundland and Labrador
 Office of the Superintendent of Securities, Northwest Territories
 Office of the Yukon Superintendent of Securities
 Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

Grace Knakowski
 Secretary
 Ontario Securities Commission
 20 Queen Street West, 22nd Floor
 Toronto, ON M5H 3S8
comments@osc.gov.on.ca

Dear Sirs/Mesdames:

**Re: Request for Comments on the Proposed National Instrument 91-102 –
*Prohibition of Binary Options and Related Proposed Companion Policy (the
 “Binary Option Prohibition”)***

The Canadian Advocacy Council¹ for Canadian CFA Institute² Societies (the CAC) appreciates the opportunity to comment on the proposed Binary Option Prohibition.

¹The CAC represents more than 15,000 Canadian members of the CFA Institute and its 12 Member Societies across Canada. The CAC membership includes portfolio managers, analysts and other investment professionals in Canada who review regulatory, legislative, and standard setting developments affecting investors, investment professionals, and the capital markets in Canada. See the CAC's website at <http://www.cfainstitute.org/cac>. Our Code of Ethics and Standards of Professional Conduct can be found at <http://www.cfainstitute.org/ethics/codes/ethics/Pages/index.aspx>.

² CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion for ethical behavior in investment markets and a respected source of knowledge in the global financial community. The end goal: to create an environment where investors' interests come first, markets function at their best, and economies grow. CFA Institute has more than 149,603 members in 163 countries, including 143,386 CFA charterholders and 148 member societies. For more information, visit www.cfainstitute.org.

We support the CSA's efforts in prohibiting the advertising, offering, selling and trading of binary options to an individual including a company that is created, or primarily used, to trade binary options. It appears evident in the preamble of the proposed Binary Option Prohibition that binary options are commonly used as vehicles to commit fraud against individuals, often with no possibility of recovering the funds. Accordingly, it is important that the CSA takes this measure in furtherance of the goal to prevent fraud and support better investor protection in the capital markets.

We provide the following comments specifically relating to the scope of the proposed Binary Option Prohibition.

First, the definition of binary options, as set out in the proposed Binary Option Prohibition, includes a contract or instrument that pays a fixed amount to the holder if the underlying interest in the contract or instrument meets a pre-determined condition, and a lesser amount or no payout if the underlying interest does not meet the pre-determined condition. Unlike other forms of derivatives, binary options do not oblige the holder to deliver or purchase the security or commodity. This definition of a binary option could potentially exclude other types of financial instruments that raise similar investor protection concerns. Accordingly, we query whether the sale of other such financial instruments to retail investors should also be restricted.

In particular, instruments such as leveraged foreign exchange over-the-counter products may give rise to the same concerns expressed in the Binary Option Prohibition and consequently we query whether they ought to fall within the ambit of this proposal. We observe that these types of instruments along with their pricing, terms, and other features are equally opaque to the retail investor.

Second, in taking regulatory action, it is important to explore the treatment of like instruments in order to ensure clarity and consistency in the capital markets. We note that the Ontario Securities Commission (OSC) published a Staff Notice in 2009 with respect to the offering of contracts for difference and foreign exchange contracts to Ontario investors (the Notice).³ In this Notice, the OSC emphasized the need for registration and reminded market participants of the prospectus requirements and exemptions when offering such products to Ontario investors, but did not take any further regulatory action with respect to banning these products. The Notice was in response to concerns raised that such instruments were being sold to retail investors by unregistered and offshore entities through the internet. Similar concerns are expressed in the proposed Binary Option Prohibition.

Third, we are of the view that binary options are fairly opaque products for the retail investor. The ability to offer such products to retail investors (provided the pre-determined condition is met in 30 days or more) may still present certain fraud risks which would inhibit the proposed ban from fully achieving its objectives.

³ See OSC Staff Notice 91-702 – Offerings of Contracts For Difference and Foreign Exchange Contracts to Investors in Ontario

Concluding Remarks

We thank you for the opportunity to provide these comments. We would be happy to address any questions you may have and appreciate the time you are taking to consider our points of view. Please feel free to contact us at chair@cfaadvocacy.ca on this or any other issue in future.

(Signed) *Michael Thom*

Michael Thom, CFA
Chair, Canadian Advocacy Council