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The Financial Services and Markets Authority (FSMA) has published a draft regulation[1] on its website which it plans to adopt. This regulation establishes a framework for the distribution of certain OTC derivative financial instruments on the Belgian retail market.

The FSMA has observed that certain types of particularly risky derivative financial instruments are distributed to retail clients in Belgium through electronic trading platforms generally located abroad. The instruments concerned are the following:

- Binary options: these are contracts under which each party undertakes to pay the other a specific amount if the price of a given asset (listed share, currency, commodity, index, precious metal, etc.) changes in the manner predicted after a lapse of time that may be very short (mere seconds or minutes);
- Rolling spot forex transactions: these are spot transactions in currencies whereby the contract is renewed indefinitely until one of the parties closes its position. The transaction is then settled in cash based on the change in the underlying currency since the time the contract was entered into;
- Contracts for difference (CFD): a CFD is an agreement between a buyer and a seller under which the parties exchange the difference between the current price of an underlying asset (listed share, currency, commodity, index, precious metal, etc.) and its price when the contract is closed.

The FSMA intends to adopt a regulation providing a framework for the distribution of such instruments. This initiative is based on the following grounds:

- The instruments mentioned above are particularly risky and even arbitrary, and have generally nothing in common with a real investment or financial transaction. Generally they are hardly if at all based on economic fundamentals and are therefore most often purely speculative. Thus they definitely do not aim to enable the investor to make an investment in the traditional sense of the word.
- These instruments are - despite their extremely high-risk nature - most often presented by their promoters as making it possible to obtain high yields at a time of historically low interest rates. However, studies in this area have shown that in reality these instruments usually result in losses for the subscribers.
- The distribution techniques used by the providers concerned are often aggressive and inappropriate, given the characteristics of this type of instrument and the risks associated with them.
- In conclusion, these instruments are not suited to being distributed to retail clients.

Since 2011 the FSMA has repeatedly published warnings about the distribution of such instruments to retail investors[2]. This phenomenon is not limited to Belgium. ESMA as well as foreign supervisors have also published several warnings in order to draw the investors’ attention to the risks associated with such instruments[3].

A report by the AMF on the results achieved by individual investors from trading in CFDs and forex in France indicates that the percentage of clients who lost money was as much as 89%[4]. The FSMA has received numerous complaints by retail investors who had sustained losses which were sometimes substantial, as a result of the distribution of these types of instruments.

It should be noted that measures have already been taken with respect to the distribution of such instruments in many countries such as the United States, Japan, Canada, Hong Kong, Poland, Singapore and Turkey. These measures are aimed at regulating or prohibiting, wholly or partially, the distribution of these types of instruments or certain distribution techniques.

For these reasons and considering that, on the one hand, the measures taken so far have not been sufficient to curb the phenomenon, and on the other hand, that the entry into force of the MiFID II Directive, enabling the FSMA to take prohibitive measures, may be postponed, the FSMA considers that restrictive measures are urgently needed.

The draft regulation is made up of two elements which will apply cumulatively.

The first element is aimed at banning the distribution of certain OTC derivative financial instruments to retail investors. This applies to instruments whose maturity is under 14 days, currency derivatives (rolling spot forex and contracts for difference on currencies), derivative instruments that comprise a significant leverage ratio greater than [5] and derivatives on non-mainstream assets (with the exception of gold)[5].

The second element identifies certain aggressive or inappropriate distribution techniques (the use of call centres for cold calling, inadequate modes of remuneration, fictitious gifts or bonuses, etc.) that were found to be used on the market. The draft regulation prohibits the use of such practices for the distribution of OTC derivative financial instruments to retail investors.

The text of this draft regulation and an explanatory commentary are annexed to this press release.

The FSMA would like to obtain reactions and comments on this initiative from all interested parties. They are invited to express their opinion on the following questions:

- Do you think, in general, that this initiative is likely to strengthen the protection of consumers of financial services and products and to improve confidence in the financial sector?
- Do you find the limitation of the use of leverage to [5] as currently proposed in the draft regulation to be sufficient or do you believe that it would be appropriate to extend the prohibition to all OTC derivatives with leverage?
- In your opinion, is it appropriate to expand the scope of this regulation to other categories of OTC derivatives (OTC derivatives without leverage and/or on shares), given the risks associated with the absence of a central counterparty and the concentration risks in this market which are difficult to measure by the retail clients, or for other reasons?
- Are there, in your view, other distribution methods than those mentioned in Article 2 of the draft regulation which should also be forbidden?

You are invited to submit your reactions in writing by email to consult1@fsma.be at the latest by **25 January 2016**. The reactions will not be published individually.

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[1] Article 30*bis* of the Law of 2 August 2002 on the supervision of the financial sector and on financial services confers on the FSMA the power to adopt regulations that, taking into account the interests of users of financial products or services, prohibit or make subject to restrictive conditions the distribution or certain forms of distribution to retail clients of financial products or certain classes of financial products. The FSMA may adopt such regulations on the advice of the Supervisory Board and after having requested the opinion of the Consumer Board (Conseil de la Consommation/Raad voor het Verbruik). These regulations enter into force only after their approval by Royal Decree and their publication in the Moniteur belge/Belgisch Staatsblad (Belgian Official Gazette).

[2] See the publications on the FSMA's website, in particular the warnings of 29 June 2011 and 2 May 2014.

[3] See the recent press release of the Netherlands Authority for the Financial Markets (AFM) “Meer meldingen van consumenten bij AFM over binaire opties en beleggen buiten toezicht”.

[4] This report is available on the AMF website. There is no reason to believe that the results would be different in Belgium.

[5] It should be noted in this regard that the draft regulation does not concern OTC derivatives intended exclusively to cover risks incurred in the course of one's professional activities.