



Conduct of Business Rulebook (COBS)

*In this attachment underlining indicates new text and striking through indicates deleted text.

23. CORE RULES – AUTHORISED PERSONS DEALING IN OTC LEVERAGED PRODUCTS

23.1 Application

The Rules in this Chapter apply to every Authorised Person with respect to the conduct of any Regulated Activity in relation to an OTC Leveraged Product.

23.2 Interpretation

In this Chapter, the following terms have the following meanings attributed to them:

“major currency” means any of the following:

- (i) U.S. Dollar;
- (ii) Euro;
- (iii) Japanese Yen;
- (iv) Pound Sterling;
- (v) Swiss Franc;
- (vi) Canadian Dollar;
- (vii) Australian Dollar; or
- (viii) New Zealand Dollar;

“major equity indices” means any index identified in the table below:

<u>Country</u>	<u>Index</u>
<u>Australia</u>	<u>All Ordinaries</u>
<u>Austria</u>	<u>Austrian Traded Inde`x</u>
<u>Belgium</u>	<u>BEL 20</u>
<u>Canada</u>	<u>TSE 35, TSE 100, TSE 300</u>
<u>France</u>	<u>CAC 40, SBF 250</u>
<u>Germany</u>	<u>DAX</u>
<u>European Union</u>	<u>Dos Jones Stoxx 50 Index, FTSE Eurotop 300, MCSI Euro Index</u>
<u>Hong Kong</u>	<u>Hang Seng</u>
<u>Italy</u>	<u>MIB 30</u>
<u>Japan</u>	<u>Nikkei 225, Nikkei 300, TOPIX</u>
<u>Korea</u>	<u>Kospi</u>

<u>Country</u>	<u>Index</u>
<u>Netherlands</u>	<u>AEX</u>
<u>Singapore</u>	<u>Straits Times Index</u>
<u>Spain</u>	<u>IBEX 35</u>
<u>Sweden</u>	<u>OMX</u>
<u>Switzerland</u>	<u>SMI</u>
<u>United Kingdom</u>	<u>FTSE 100, FTSE Mid 250, FTSE All Share</u>
<u>United States of America</u>	<u>S&P 500, Dow Jones Industrial Average, NASDAQ Composite, Russell 2000</u>

“margin” means the means the amount of Money a Retail Client has agreed to pay to the Authorised Person in order to open a position in relation to an OTC Leveraged Product;

“non-major currency” means any currency which is not a major currency.

“relevant sovereign debt” means an issue of public debt by or on behalf of:

- (i) the United Kingdom;
- (ii) the United States of America;
- (iii) France;
- (iv) Australia;
- (v) Germany;
- (vi) Japan;
- (vii) Canada;
- (viii) Switzerland; or
- (ix) a member state of the EU that has adopted the Euro as its currency.

“rolling spot forex contract” means a contract for difference where the value of the contract is ultimately determined by reference, wholly or in part, to fluctuations in an exchange rate or the value of a currency.

23.3 Marketing Materials

An Authorised Person must include sufficiently prominent and clear links to the risk disclosure statement containing the information set out in Rule 23.4(3) on the main page of its website, in all marketing and educational materials, other communications channels and as part of each risk warning or disclaimer that appears on its website.

23.4 Risk Disclosure Statement

23.4.1 Before an Authorised Person opens a trading account enabling a Retail Client to buy and sell OTC Leveraged Products, it must:

- (a) provide a separate risk disclosure statement, as described in Rule 23.4.3, to Retail Clients as part of the onboarding process in good time before the Authorised Person carries on any business for a Retail Client;
- (b) obtain a documented acknowledgement from such Retail Client that they have received and reviewed the risk disclosure statement and fully understand and accept the risks involved in trading in OTC Leveraged Products;
- (c) provide a duplicate copy of the documented acknowledgement to each Retail Client; and
- (d) maintain a record of the acknowledgment in (b) in accordance with applicable record keeping requirements.

23.4.2 The risk disclosure statement must also be:

- (a) provided on an annual basis to each Retail Client; and
- (b) published and available at all times on the website of the Authorised Person.

23.4.3 A risk disclosure statement provided by an Authorised Person to a Retail Client in accordance with Rule 23.4.1 must include a prominent warning that investing in OTC Leveraged Products involves the risk of losing substantially more than the initial margin posted by the Retail Client, and further state that:

- (a) the risk disclosure statement may not identify or address all risks associated with OTC Leveraged Products;
- (b) the Retail Client is at risk of losing all of their capital outlay and any profits not redeemed;
- (c) the Retail Client is at risk of losing money and accumulating losses rapidly;
- (d) margin trading and use of leverage amplifies losses when they occur;
- (e) margin-trading limits, stop-loss limits, or other systems and controls designed to mitigate or limit loss exposures may not be effective or may fail. Where relevant, an explanation of stop-loss orders, which must include clear information about whether or not a stop-loss is “guaranteed” (i.e. it would operate whatever the market circumstances are), and that in the case that it is not guaranteed, it may not limit Retail Client losses in the event of highly volatile trading conditions in an underlying asset or reference price;
- (f) the risk of slippage, i.e. a divergence between the price at which a trade was approved and the price at which it was executed; and
- (g) most Retail Clients transacting in OTC Leveraged Products lose money.

23.4.4 The risk disclosure statement must include a prominent display of performance data for each relevant OTC Leveraged Product that clearly identifies the

percentage of active Retail Client accounts that were profitable. For the purposes of this disclosure:

- (a) active accounts include the total number of Retail Client accounts in which that specific OTC Leveraged Product was traded or held during that period;
- (b) profitable accounts include each active account for which net trading activity involving only that specific OTC Leveraged Product resulted in a realised profit, excluding any bonus or promotional amount, for that period; and
- (c) the performance data must state separately each of the four most recently completed calendar quarters or, where the Authorised Person has not yet completed four calendar quarters of offering OTC Leveraged Products to Retail Clients, those calendar quarters that have been completed.

23.4.5 The risk disclosure statement must state that it is the responsibility of the Retail Client:

- (a) to consider whether the products are suitable for them and whether they can afford to risk all of their capital outlay; and
- (b) to consult with their own legal and other professional advisors before committing to any transaction, signing any documents and/or entering into any legally binding arrangement in relation to these products.

23.4.6 The risk disclosure statement must state whether the Authorised Person has any actual or potential conflicts of interest with their Retail Clients, including placing the interests of the Retail Client first, and clearly identify:

- (a) what those conflicts of interest are, or may be;
- (b) any potential, associated benefits for the Authorised Person;
- (c) the right of the Retail Client to object to those conflicts of interest; and
- (d) the Authorised Person's obligation to request a positive written affirmation from the Retail Client as to whether or not they accept the actual or potential conflicts of interest.

23.4.7 The risk disclosure statement must provide details of the Regulator of the Authorised Person.

23.4.8 All information provided or made available by the Authorised Person to a Retail Client in accordance with this Chapter must be provided or made available in English or the language they are most likely to comprehend, using easily understandable language and in a clear and comprehensible form.

Guidance

1. The requirements in this section specify the minimum information that an Authorised Person must communicate to its Retail Clients and it should consider whether there is any additional information that should be disclosed to them.
2. The risk disclosure statement should not be longer than three A4 size pages, including any diagram or numerical illustration, but excluding the Retail Client's acknowledgement. Information in the short-form disclosure fact sheet (including

footnotes) shall be presented in a font size of at least 10-point Calibri or Times New Roman.

23.5 Appropriateness Assessment

23.5.1 An Authorised Person must not offer OTC Leveraged Products to a Retail Client, or provide any advice or make arrangements on behalf of a Retail Client relating to OTC Leveraged Products unless it has first completed an assessment of the skill, experience, knowledge, financial resources and risk tolerance of the Retail Client, such that the Authorised Person may reasonably conclude that the Retail Client has:

- (a) adequate experience and skill enabling them to understand the potential risk of loss involved in investing in OTC Leveraged Products; and
- (b) liquid financial resources sufficient to absorb potential losses resulting from trading in OTC Leveraged Products.

Guidance

1. In order to satisfy the requirements imposed by Rule 23.5.1, the Authorised Person should, prior to establishing a business relationship with a Retail Client, consider whether such Retail Client demonstrates an understanding of the risks and potential magnitude of losses which they may be exposed to.
2. In order to gain such understanding, the Authorised Person should consider the trading history of the Retail Client, including the volume of that trading, as well as any relevant professional qualifications the Retail Client might have. The Authorised Person should also seek information concerning the liquid financial resources of the Retail Client, which will enable them to absorb losses which may result from trading in OTC Leveraged Products, including whether the Retail Client may be able to absorb losses arising from their contemplated investments without needing to resort to credit facilities.

23.5.2 The assessment required by Rule 23.5.1 must be reassessed by an Authorised Person:

- (a) on an annual basis; or
- (b) where there is any material change in the financial situation or risk tolerance of the Retail Client, if that change occurs prior to the annual reassessment.

23.6 Margin Requirements for Retail Clients

An Authorised Person must require a Retail Client to have posted margin, in the form of Money, before it opens a position in an OTC Leveraged Product for that Retail Client of at least the following proportion of the value of the exposure of the Retail Client:

- (a) 3.33% for major currency pairs and relevant sovereign debt;
- (b) 5% for non-major currency pairs, gold and major equity indices;
- (c) 10% for commodities, excluding gold, and non-major equity indices;
- (d) 20% for individual equities; or

- (e) 50% for Virtual Assets.

Guidance

1. The funds in the account of a Retail Client consist of the margin deposited in the account for the purpose of trading OTC Leveraged Products plus unrealised net profits from open positions in them, the latter taken as the sum of unrealised gains and losses of all open positions recorded in the account. Any cash or other assets in the account for purposes other than trading OTC Leveraged Products do not represent funds available to meet the above margin requirements.
2. Margin deposited in the account of a Retail Client to meet a margin requirement above in relation a position in an OTC Leveraged Product may not be used to meet a margin requirement in relation to any other OTC Leveraged Products.

23.7 Margin close-out Requirements for Retail Clients

23.7.1 An Authorised Person must ensure that “net equity” of a Retail Client in an account used to trade OTC Leveraged Products does not fall below 50% of the margin requirement, as outlined in COBS 23.6, required to maintain the Retail Client’s open positions.

23.7.2 Where the net equity of a Retail Client falls below 50% of the margin requirement, the Authorised Person must close the Retail Client’s open position(s) in OTC Leveraged Products as soon as market conditions allow.

Guidance

In this Rule, “net equity” means the sum of the deposited margin and the unrealised net profit and loss on open positions in that account.

23.8 Negative Balance Protection

The liability of a Retail Client for all their investments in OTC Leveraged Products connected to their account is limited to the funds in that account maintained for the purpose of trading OTC Leveraged Products.

Guidance

1. Funds in the account of a Retail Client are limited to the then current amount of deposited margin in the account plus all unrealised net profits from open positions.
2. Any cash or other assets in the account for purposes other than trading OTC Leveraged Products do not represent funds available to meet the liability.

23.9 Prohibition of Incentives

An Authorised Person must not offer promotions, bonuses or other inducements to Retail Clients in connection with the offer or sale of OTC Leveraged Products, whether monetary or non-monetary in nature.

23.10 Promotion by Third Parties and Referrals

23.10.1 An Authorised Person must have systems and controls in place to ensure that introducing brokers are not actively promoting OTC Leveraged Products and that Retail Client acquisition does not involve the provision of investment advice or portfolio management on behalf of the Authorised Person.

23.10.2 An Authorised Person must not accept a referral of a Retail Client made by an unregulated Person for reward.

23.10.3 An Authorised Person must have adequate systems and controls to ensure compliance with Rule 23.10.2.

Guidance

For the purposes of Rule 23.10.2, an “unregulated Person” means a Person that is not an Authorised Person or a Regulated Financial Institution.

23.11 Liquidity Providers

An Authorised Person must, in relation to liquidity providers:

- (a) undertake an assessment and conclude that the liquidity providers used are suitable to provide liquidity to its Retail Clients;
- (b) ensure that the best price is available from liquidity providers for its Retail Clients, including under extreme market conditions;
- (c) at all times retain more than one liquidity provider in order to better discharge the requirement stated in (b); and
- (d) undertake independent monitoring of the quality of the orders executed by liquidity providers on behalf of its Retail Clients.

23.12 Additional Restrictions relating to OTC Leveraged Products

23.12.1 The Applicant must not offer or sell to Retail Clients OTC Leveraged Products which:

- (a) relate to underlying non-financial instruments or non-commodities, binary options or analogous products;
- (b) do not have a transparent pricing mechanism available for determining the price movement of the underlying reference, by which the profit or loss of each party to the OTC Leveraged Product may be determined;
- (c) do not have a two-way pricing mechanism that permits the Retail Client to trade at the prices quoted during the currency of the OTC Leveraged Product.

23.12.2 An Authorised Person must not offer or arrange for Retail Clients to subscribe to “copy trading,” “mirror trading,” or similar services unless it holds a Financial Services Permission to undertake the Regulated Activity of Managing Assets and has implemented, to the satisfaction of the Regulator, effective systems and controls and governance to identify and manage all related material risks.

23.12.3 An Authorised Person must ensure, to the extent possible, that a Retail Client does not fund its account through the use of a credit card or a third party credit facility.