THIS TEXT IS A TRANSLATION OF THE DECISION IN DUTCH. IN CASE OF DIFFERENCES THE DECISION IN DUTCH PREVAILS.

Decision dated 18 April 2019, to temporarily restrict the marketing, distribution or selling of contracts for differences to retail clients in accordance with Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 and the Financial Supervision Act (**CFD Restrictions**).

The Dutch Authority for the Financial Markets, having regard to,

Article 42 of Regulation (EU) No. 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012;
Article 21 of the Commission Delegated Regulation (EU) 2017/567 of 18 May 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regard to definitions, transparency, portfolio compression and supervisory measures on product intervention and positions;
Article 1:77f of the Financial Supervision Act; and
Article 2, first paragraph, opening lines and part m, of the EU Financial Markets Regulations (Implementation) Decree,

decides:

Article 1
Definitions
For the purpose of application of this decisions, the terms below are defined as follows:

1. ‘contract for differences’ or ‘CFD’ means a derivative other than an option, future, swap or forward rate agreement, the purpose of which is to give the holder a long or short exposure to fluctuations in the price, level or value of an underlying value, irrespective of whether it is traded on a trading venue, and that must be settled in cash or may be settled in cash at the option of one of the parties other than by reason of default or other termination event;
2. ‘excluded non-monetary benefit’ means any non-monetary benefit other than, insofar as they relate to CFDs, information and research tools;
3. ‘initial margin’ means any payment for the purpose of entering into a CFD, excluding commission, transaction fees and any other related costs;
4. ‘initial margin protection’ means the initial margin determined by Annex I;
5. ‘margin close-out protection’ means the closure of one or more of a retail client's open CFDs on terms most favourable to the client in accordance with Articles 24 and 27 of Directive 2014/65/EU when the sum of funds in the CFD trading account and the unrealised net profits of all open CFDs connected to that account falls to less than half of the total initial margin protection for all those open CFDs;
6. ‘negative balance protection’ means the limit of a retail client's aggregate liability for all CFDs connected to a CFD trading account with a CFD provider to the funds in that CFD trading account.
7. ‘offering’: marketing, distributing or selling; and
8. ‘provider’: the person that offers.

Article 2

Restrictions on CFDs in respect of retail clients

The marketing, distribution or sale to retail clients of CFDs is restricted to circumstances where at least all of the following conditions are met:

1. the CFD provider requires the retail client to pay the initial margin protection;
2. the CFD provider provides the retail client with the margin close-out protection;
3. the CFD provider provides the retail client with the negative balance protection;
4. the CFD provider does not directly or indirectly provide the retail client with a payment, monetary or excluded non-monetary benefit in relation to the marketing, distribution or sale of a CFD, other than the realised profits on any CFD provided; and
5. the CFD provider does not send directly or indirectly a communication to or publish information accessible by a retail client relating to the marketing, distribution or sale of a CFD unless it includes the appropriate risk warning specified by and complying with the conditions in Annex II.

Article 3

Prohibition of participating in circumvention activities

It shall be prohibited to participate, knowingly and intentionally, in activities the object or effect of which is to circumvent the requirements in Article 2, including by acting as a substitute for the CFD provider.

Article 4

Entry into force

This Decision enters into force on 19 April 2019.

Done in Amsterdam on 18 April 2019

Annex I

INITIAL MARGIN PERCENTAGES BY TYPE OF UNDERLYING

a) 3.33% of the notional value of the CFD when the underlying currency pair is composed of any two of the following currencies: US dollar, Euro, Japanese yen, Pound sterling, Canadian dollar or Swiss franc;

b) 5% of the notional value of the CFD when the underlying index, currency pair or commodity is:
   i. any of the following equity indices: Financial Times Stock Exchange 100 (FTSE 100); Cotation Assistée en Continu 40 (CAC 40); Deutsche Bourse AG German Stock Index 30 (DAX30); Dow Jones Industrial Average (DJIA); Standard & Poors 500 (S&P 500); NASDAQ Composite Index (NASDAQ), NASDAQ 100 Index (NASDAQ 100); Nikkei Index (Nikkei 225); Standard & Poors/Australian Securities Exchange 200 (ASX 200); EURO STOXX 50 Index (EURO STOXX 50);
   ii. a currency pair composed of at least one currency that is not listed in point (a) above; or
   iii. gold;

c) 10% of the notional value of the CFD when the underlying commodity or equity index is a commodity or any equity index other than those listed in point (b) above;

d) 50% of the notional value of the CFD when the underlying asset is a cryptocurrency; or

e) 20% of the notional value of the CFD when the underlying asset is:
   i. a share; or
   ii. not otherwise listed in this Annex.

Annex II

RISK WARNINGS
SECTION A
Risk warning conditions

1. The risk warning shall be in a layout ensuring its prominence, in a font size at least equal to the predominant font size and in the same language as that used in the communication or published information.
2. If the communication or published information is in a durable medium or a webpage, the risk warning shall be in the format specified in Section B.
3. If the communication or information is in a medium other than a durable medium or a webpage, the risk warning shall be in the format specified in Section C.
4. The risk warning shall include an up-to-date provider-specific loss percentage based on a calculation of the percentage of CFD trading accounts provided to retail clients by the CFD provider that lost money. The calculation shall be performed every 3 months and cover the 12-month period preceding the date on which it is performed ('12-month calculation period'). For the purposes of the calculation:
    a) an individual retail client CFD trading account shall be considered to have lost money if the sum of all realised and unrealised net profits on CFDs connected to the CFD trading account during the 12-month calculation period is negative;
    b) any costs relating to the CFDs connected to the CFD trading account shall be included in the calculation, including all charges, fees and commissions;
    c) the following items shall be excluded from the calculation:
        i. any CFD trading account that did not have an open CFD connected to it within the calculation period;
        ii. any profits or losses from products other than CFDs connected to the CFD trading account;
        iii. any deposits or withdrawals of funds from the CFD trading account.
5. By way of derogation from paragraphs 2 to 4, if in the last 12-month calculation period a CFD provider has not provided an open CFD connected to a retail client CFD trading account, that CFD provider shall use the standard risk warning specified in Sections D and E, as appropriate.
6. If the communication or published information is drawn up in a language other than the Dutch language, the CFD provider will apply for the purpose of the risk warning the corresponding text as published in that other language in Annex 2 to the European Securities and Markets Authority Decision (EU) 2018/796 of 22 May 2018 to temporarily restrict contracts for differences in the Union in accordance with Article 40 of Regulation (EU) No 600/2014 of the European Parliament and of the Council.

SECTION B
Durable medium and webpage provider-specific risk warning

CFDs are complex instruments and come with a high risk of losing money rapidly due to leverage. [insert percentage per provider] % of retail investor accounts lose money when trading CFDs with this provider. You should consider whether you understand how CFDs work and whether you can afford to take the high risk of losing your money.

SECTION C
Abbreviated provider-specific risk warning

[insert percentage per provider] % of retail investor accounts lose money when trading CFDs with this provider. You should consider whether you can afford to take the high risk of losing your money.

SECTION D
Durable medium and webpage standard risk warning

CFDs are complex instruments and come with a high risk of losing money rapidly due to leverage. Between 74-89 % of retail investor accounts lose money when trading CFDs. You should consider whether you understand how CFDs work and whether you can afford to take the high risk of losing your money.

SECTION E
Abbreviated standard risk warning

Between 74-89 % of retail investor accounts lose money when trading CFDs. You should consider whether you can afford to take the high risk of losing your money.

Explanation

1. Introduction

1) In recent years, the European Securities and Markets Authority (**ESMA**) and several competent authorities in Member States of the European Union (NCAs) including the Dutch Authority for the Financial Markets (**AFM**) have observed a rapid increase in the marketing, distribution or sale of CFDs to non-professional clients (**retail clients**) across the European Union (**EU**). CFDs are inherently risky and complex products and are often traded speculatively. ESMA and the NCAs have also observed that the offering of CFDs to retail clients has been increasingly characterized by aggressive marketing techniques as well as a lack of transparent information that do not allow retail clients to understand the risks underlying these products. ESMA and the NCAs also established in recent years an increase in the number of retail clients that trades in these products and loses money. This increase was accompanied over the past years by numerous complaints from retail clients from all over the EU who sustained considerable losses trading in CFDs.

2) In the past, the AFM pointed out the risks inherent in trading in CFDs on several occasions. In 2011, the AFM already took over a warning from ESMA concerning the risks of CFDs.[1] In 2015, the AFM concluded in the report pursuant to the CFD product investigation that providers[2] of CFDs expose investors unnecessarily to risks.[3] In 2017, the AFM also consulted the market regarding an advertising prohibition of (inter alia) CFDs with a leverage of 10 or higher.[4] The AFM informed the market on 8 January 2019 that it is investigating whether it is necessary to implement national measures with respect to the sale in or from the Netherlands of binary options and CFDs.[5] The AFM informed the public on 7 March 2019 that it is preparing a ban on binary options and restrictions on CFDs in the Netherlands.[6] ESMA has also been publishing warnings for several years in which it emphasises its concerns with respect to the risks of the uncontrolled offer of CFDs to retail clients.[7]

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[1] 'European Supervisor ESMA warns investors', 7 December 2011, https://www.afm.nl/en/nieuws/2011/dec/esma-waarschuwing-beleggers.

[2] As defined in Article 1, eighth paragraph of this decision.

[3] 'AFM: 'Providers of Contracts for Difference unnecessarily expose investors to risks', 13 February 2015, https://www.afm.nl/en/nieuws/2015/feb/rapport-cfds.

[4] 'Consultation: AFM prepares for ban on advertising of harmful financial products', 20 February 2017, https://www.afm.nl/nl-nl/nieuws/2017/feb/consultatie-reclameverbod.

[5] 'ESMA verlengt verbod op binaire opties en beperkingen op CFD's', 8 January 2019, https://www.afm.nl/nl-nl/professionals/nieuws/2019/jan/verlenging-verbod-binaire-opties.

[6] 'AFM bereidt verbod voor op binaire opties en beperkingen aan CfD's in Nederland', 7 March 2019 https://www.afm.nl/nl-nl/professionals/nieuws/2019/mrt/interventies-binaire-opties-cfds.

[7] Warning issued by ESMA and EBA to investors concerning „contracts for difference (CFD's)", 28 February 2013, https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-267.pdf; ESMA investor warning „Risks of investing in complex products", 7 February 2014, https://www.esma.europa.eu/sites/default/files/library/2015/11/investor_warning_-_complex_products_20140207_-_en_0.pdf; ESMA investor warning concerning „Warning about CFDs, binary options and other speculative products" of 25 July 2016 (available at: https://www.esma.europa.eu/sites/default/files/library/2016-1166_warning_on_cfds_binary_options_and_other_speculative_products_0.pdf).

3) The grave concerns about the protection of investors caused ESMA to decide[8] on 22 May 2018 to temporarily restrict marketing, distributing or selling CFDs in the Union in accordance with Article 40 of Regulation (EU) No 600/2014 of the European Parliament and of the Council (**ESMA Decision**). This measure entered into force on 1 August 2018 and will has since been extended three times each time by a period of three months. [9] Prior to the ESMA Decision, ESMA published[10] a ´Call for Evidence´ on 18 January 2018 in which it consulted the market about the possible product intervention measures relating to the marketing, distribution or sale of binary options and CFDs to retain clients (**Call for Evidence**).

4) The AFM endorses the considerations in the ESMA Decision to support the restrictive measures imposed by ESMA. As evident from the considerations in paragraph 3.1, the AFM reaches the same conclusion as ESMA, which is that CFDs give rise to significant investor protection concerns. The AFM is also of the opinion that it is unacceptable in the current state of affairs if CFDs were marketed, distributed or sold to retail clients (again) without restriction.

5) The AFM therefore considers it necessary to restrict the marketing, distribution or sale of CFDs to retail clients in or from the Netherlands in accordance with Article 42 of Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (**MiFIR**) and Article 1:77f of the Financial Supervision Act (**Wft**). The restrictions apply to investment firms that have their registered office in the Netherlands and to investment firms that have their registered office in another Member State who provide investment services in the Netherlands by means of a branch office or via the free provision of services on the basis of a European passport. The restrictions also apply to investment firms with their registered office in the Netherlands that provide investment services in another Member State. The restrictions apply for an indefinite period. The AFM will revoke the restrictions as soon as the conditions set out in Article 42, second paragraph, MiFIR no longer apply.

6) The AFM did not consult with the market regarding the present decision, because a public consultation or consultation of relevant market parties is not required on the basis of Article 42 MiFIR. What is more, market parties were already afforded the opportunity to respond to ESMA's Call for Evidence. The present AFM measure does not deviate from the ESMA Decision.

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[8] European Securities and Markets Authority Decision (EU) 2018/796 of 22 May 2018 to temporarily restrict the marketing, distribution or sale of contracts for differences (CFDs) to retail clients in the Union in accordance with Article 40 of Regulation (EU) No 600/2014 of the European Parliament and of the Council. https://eur-lex.europa.eu/legal-content/NL/TXT/?uri=CELEX:32018X0601(02).

[9] 'ESMA to renew restriction on CFDs for a further three month', 28 September 2018, https://www.esma.europa.eu/press-news/esma-news/esma-renew-restriction-cfds-further-three-months, "ESMA to renew restrictions on CFDs for a further three months from 1 February 2019", 19 December 2018, https://www.esma.europa.eu/press-news/esma-news/esma-renew-restrictions-cfds-further-three-months-1-february-2019, and 'ESMA to renew restrictions on CFDs for a further three months from 1 May 2019', 27 March 2019, https://www.esma.europa.eu/press-news/esma-news/esma-renew-restrictions-cfds-further-three-months-1-may-2019.

[10] 'Call for Evidence – Potential product intervention measures on contracts for differences and binary options to retail clients', 18 January 2018, https://www.esma.europa.eu/press-news/consultations/call-evidence-%E2%80%93-potential-product-intervention-measures-contracts.

The AFM notes in conclusion that it took account of the points presented by ESMA concerning the responses that were received in the present decision.

7) In order to remove any doubt, the terminology and definitions in this decision – unless explicitly stated otherwise – have the same meaning as in the Wft, Regulation 2014/65/EU of the European Parliament and of the Council 15 May 2014 on markets for financial instruments and amending Directives 2002/92/EC and 2011/61/EU (**MiFID II**) and MiFIR.

8) This decision applies to investment firms, authorised under MiFID II and credit institutions authorised under Directive 2013/36/EU of the European Parliament and of the Council (Capital Requirements Regulation) when providing investment services and/or performing investment activities, and to market operators including any trading platforms the operate.[11]

9) The present AFM decision satisfies the conditions set out in Article 42 MiFIR. The AFM explains this as follows in this decision:

- Chapter 2 describes the scope of this decision.
- Chapter 3 describes the basis on which the AFM concludes that the conditions of Article 42, second paragraph, MiFIR have been satisfied.
    i. Paragraph 3.1 describes the existence of a significant cause for concern about investor protection (Article 42, second paragraph, under a, point i, MiFIR).
    ii. Paragraph 3.2 describes the applicable, existing requirements on the basis of Union law and that do not and cannot remove the concern about investor protection (Article 42, second paragraph, under b, MiFIR).
    iii. Paragraph 3.3 describes the proportionality of this decision (Article 42, second paragraph, under c, MiFIR).
    iv. Paragraph 3.4 describes the AFM's consultation of the NCAs in other Member States that may be significantly effected by this decision (Article 42, second paragraph, under d, MiFIR).
    v. Paragraph 3.5 describes the absence of a discriminatory effect on services and activities that are provided from another Member State (Article 42, second paragraph, under e, MiFIR).
    vi. Paragraph 3.6 describes the AFM's consultation with the public body competent for the oversight, administration and regulation of the physical agricultural markets (Article 42, second paragraph, under f, MiFIR).
- Chapter 4 describes the manner in which the AFM has notified all other NCAs and ESMA of the present measure (Article 42, paragraph 3, MiFIR).
- Chapter 5 describes the manner of publication of the notification of the present decision (Article 42. paragraph 5, MiFIR).

2. Scope of application

10) This Decision relates to CFDs that are cash-settled derivative contracts, the purpose of which is to give the holder an exposure, which can be long or short, to fluctuations in the price, level or

[11] See Article 1, second paragraph, MiFIR.

value of an underlying value. These CFDs include, inter alia, rolling spot forex products and financial spread bets.

11) Only CFDs as defined in Article 1 of this decision come under scope of application of this decision. This Decision does not relate to options, futures, swaps, and forward-rate agreements. Nor does the scope of application of this decision include warrants and turbo certificates. Similarly to ESMA, the AFM acknowledges that there are similarities between CFDs, warrants and turbo certificates, but points out these products differ from each other in various respects. The AFM will monitor closely whether similar detrimental consequences occur for retail clients in connection with the offering of these products in or from the Netherlands and it will take action if necessary. Securitised derivatives that are CFDs are not explicitly excluded from the definition of CFDs.

3. The conditions for restrictions (Article 42, second paragraph, MiFIR)

12) Article 42, second paragraph, MiFIR, includes the conditions for implementing product intervention on the basis of Article 42 MiFIR and Article 1:77f Wft. The abovementioned articles authorise the AFM to restrict the marketing, distribution or sale of CFDs if it concludes on reasonable grounds that all conditions of the second paragraph of Article 42 MiFIR have been satisfied. This chapter includes the AFM's substantiation of the present decision in which the AFM explains for each condition why it concludes that this condition has been satisfied.

3.1 Significant cause for concern about investor protection (Article 42, second paragraph, under a, point i, MiFIR)

13) The first condition that is imposed by Article 42, second paragraph, under a, MiFIR is that the AFM concluded on reasonable grounds that CFDs constitute a significant cause for concern regarding investor protection. In order to determine whether there is a significant cause for concern regarding investor protection, the AFM assessed the criteria and factors listed in Article 21, second paragraph, under (a) up to and including (v), Delegated Regulation (EU) 2017/567 of 18 May 2016 (**Delegated Regulation**). Taking into account all criteria and factors, the AFM concludes that there is a significant cause for concern regarding investor protection. The AFM explains this below on the basis of the relevant criteria and factors.

3.1.1 The degree of complexity and transparency of CFDs (Article 21, second paragraph, under (a), Delegated Regulation)

14) CFDs are complex products, typically not traded on a trading venue. The pricing, trading terms, and settlement of such products is not standardised, impairing retail clients' ability to understand the terms of the product. In addition, CFD providers often require clients to acknowledge that the reference prices used to determine the value of a CFD may differ from the price available in the respective market where the underlying value is traded, making it difficult for retail clients to check and verify the accuracy of the prices received from the provider.

15) The costs and charges applicable to trading in CFDs are complex and lack transparency for retail clients. In particular, retail clients typically find it difficult to understand and assess the expected performance of a CFD, also taking into account the complexity arising from the impact of transaction fees on such performance. Transaction fees in CFDs are normally applied to the full notional value of the trade and investors consequently incur higher transaction fees relative to their invested funds at higher levels of leverage. Transaction fees are usually deducted from the initial margin deposited by a client and high leverage can lead to a situation where the client, at the moment of opening a CFD, observes a significant loss on their trading account, caused by the application of high transaction fees. Since transaction fees at higher leverage will erode more of the client's initial margin, clients will be required to earn more money from the trade itself to realise a profit. This lowers the client's chances of realising a profit net of transaction fees, exposing clients to a greater risk of loss.

16) In addition to transaction fees, spreads and various other financing costs and charges may be applied. These include commissions (a general commission or a commission on each trade, or on opening and closing a CFD account) and/or account management fees. Financing charges are also usually applied to keep a CFD open, such as daily or overnight charges, to which a mark-up can also be added. The number and complexity of the various costs and charges and their impact on clients' trading performance contribute to the lack of sufficient transparency in relation to CFDs in order to enable a retail client to make an informed investment decision.

17) Another complexity arises from the use of stop loss orders. This product feature may give retail clients the misleading impression that a stop loss order guarantees execution at the price which they have set (the level of the stop loss). However, stop loss orders do not guarantee a protection level but the triggering of a 'market order' when the CFD price reaches the price set by the client. Accordingly, the price received by the client (execution price) can be different from the price at which the stop loss was set. While stop losses are not unique to CFDs, leverage increases the sensitivity of an investor's margin to price movements of the underlying value increasing the risk of risk of sudden losses and means that traditional trading controls such as stop losses are insufficient to manage investor protection concern.

18) Another key complexity associated with CFDs may arise from the relevant underlying market. For instance, with FX trading, clients speculate on one currency against another. If neither of these currencies is the currency used by the client to open a CFD position, any return received by the client will be dependent on the measures taken by the client to assess the movement of these three currencies. This suggests that a high level of knowledge of all the currencies involved is required to successfully navigate the complexities of such currency trading. Retail clients do not normally have such knowledge.

19) CFDs with cryptocurrencies as an underlying value raise separate and significant concerns. Cryptocurrencies are a relatively immature asset class that pose major risks for investors. The AFM warned of the risk of investing in cryptocurrencies in 2017.[12] ESMA and other regulators

[12]'Wat zijn de risico's van investeren in virtuele valuta', 21 July 2017, https://www.afm.nl/nl-nl/nieuws/2017/juni/virtuele-valuta.

have also repeatedly warned of the risks involved with investing in cryptocurrencies.[13] Many of these concerns remain present for CFDs on cryptocurrencies. This is because retail clients typically do not understand the risks involved when speculating on an extremely volatile and relatively immature asset class, which are exacerbated by trading on margin, as it requires clients to react in a very short time period. Due to the specific characteristics of cryptocurrencies as an asset class, the restrictions with respect to CFDs with cryptocurrencies as underlying value set out in this decision will be monitored very closely and reviewed if deemed necessary.

20) The high level of complexity, poor degree of transparency, nature of risks and type of underlying value confirm that a significant investor protection concern exists in respect of these CFDs.

3.1.2 The particular features or components of CFDs (Article 21, second paragraph, under (e), Delegated Regulation)

21) The main feature of CFDs is their ability to operate on leverage. In general, whilst leverage can increase the possible profit for clients, it can also increase the possible losses. In 2017, the AFM conducted an investigation among CFD providers who have their registered office or a branch in the Netherlands. In 2018, the AFM conducted an investigation among providers who offer CFDs to retail clients in the Netherlands that have their registered office in another Member State. The investigations show that leverage levels of CFDs vary from 1: 1 to 100:1 and higher. As far as retail clients are concerned, the application of leverage may increase the probability of a larger loss to a greater extent than the probability of a larger gain for the reasons set out below.

22) Leverage affects an investment's performance by increasing the impact of transaction fees incurred by retail clients.

23) Another risk related to trading in leveraged products is linked to the interaction of high leverage and the practice of automatic margin close-out. Under commonly applied contractual terms, CFD providers are granted the discretion to close-out a client's account once the client's net equity reaches a specified percentage of the initial margin that the client is required to pay in order to open a CFD position(s).

24) The interaction between high leverage and automatic margin close-out is that it increases the probability that a client's position will be closed automatically by the CFD provider in a short timeframe or a client has to post additional margin in the hope of turning around a losing position. High leverage increases the probability that the client has insufficient margin to support their open CFDs by making the client's position(s) sensitive to small fluctuations in the price of the underlying value to the client's disadvantage.

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[13] See for example the joint warning from ESMA, EBA and Eiopa concerning virtual currencies, available at: https://eiopa.europa.eu/Publications/Other%20Documents/Joint%20ESAs%20Warning%20on%20Virtual%20Currencies_NL.pdf and the EBA warning from 2013, available at: https://www.eba.europa.eu/documents/10180/598344/EBA+Warning+on+Virtual+Currencies.pdf. See also the IOSCO webpage for a list of warnings from supervisory authorities concerning virtual currencies and initial coin offerings, available at: http://www.iosco.org/publications/?subsection=ico-statements.

25) It follows from the ESMA Decision that ESMA observes that in market practice, margin close-out appears to have been introduced by CFD providers mainly to allow them to more easily manage client exposures and the provider's credit risk by closing out a client's position before the client had insufficient funds to cover their current exposure. Automatic margin close-out also provides a degree of protection for clients as it reduces, but does not eliminate, the risk that the client (particularly at high levels of leverage) loses all or more than their initial margin.

26) The AFM has observed that the level at which an automatic margin close-out was applied before the ESMA Decision entered into force varies. CFD providers with clients who typically trade at lower value order sizes, and who typically act as direct counterparty to the clients' trades, have previously set the margin close-out rule between 0 and 30% of initial margin required. By eroding the client's funds close to 0, the provider is placing the client at increased risk of losing more money than they had invested. Some NCAs also observe that it is standard market practice to apply margin close-out on a per account basis. This means that minimum margin requirements are applied based on the combined margin required for all a client's open positions connected to the CFD account, including across different asset classes. This allows profitable positions to offset losing positions across the client's account.

27) A related risk of leverage is that it places clients at risk of losing more money than they have invested. This is a key risk which retail clients may not understand, despite written warnings. The margin posted by a client is posted as collateral to support the client's position. If the price of the underlying value, for example, moves against the client's position in excess of the initial margin posted, the client can be liable for losses in excess of the funds in their CFD trading account, even after the closure of all their other open CFD positions.

28) Trading at high leverage levels also increases the impact of ‘gapping’ during periods of significant market volatility (for example the Sterling flash crash and Swiss franc de-pegging). Gapping occurs when there is a sudden movement in the price of the underlying value. Gapping is not unique to CFDs, but the risks related to such events are exacerbated by high leverage. If gapping occurs, the client on the losing side may be unable to close an open CFD at their preferred price and can result in significant client losses when trading at high leverage. In the case of the Swiss franc shock in 2015 for example, this led to retail clients losing significantly more than the sum initially invested.

29) The often high levels of leverage offered to retail clients, the volatility of certain underlying assets, together with the application of transaction costs which impact the investment's performance, can result in rapid changes to a client's investment position. This results in the client having to take swift action to manage the risk exposure by posting additional margin to avoid the position being automatically closed out. In such instances, high leverage can lead to large losses for retail clients over a very short time span and exacerbates the risk that clients will lose more than the funds paid to trade CFDs.

30) The above factors confirm that a significant investor protection concern exists in respect of these CFDs.

3.1.3 The size of potential detrimental consequences and the degree of disparity between returns for investors and the risk of loss (Article 21, second paragraph, under (b) and (f), Delegated Regulation)

31) In 2017, the AFM received information from CFD providers who have their registered office or a branch in the Netherlands. In 2018, the AFM furthermore received information with the assistance from the NCAs in question from CFD providers with their registered office in another Member State that serve retail clients in the Netherlands. In 2018, the AFM also received information from CFD providers with their registered office in the Netherlands at ESMA's request within the context of ESMA's reconsideration of the ESMA Decision and the extension thereof. The AFM estimates on the basis of the abovementioned information that in 2018 between 55,000 and 65,000 retail clients in the Netherlands traded actively in CFDs.[14] This is estimated increase of thirty to forty percent when compared to 2017. The average result realised by retail clients trading in CFDs was negative in 2017. It is estimated[15] that the average retail client lost €1,201. The data shows a correlation between the result realised and the leverage of the CFD. The average result becomes worse as the leverage increases.

32) The abovementioned information also shows that the activities involving CFDs are cross-border in nature. Retail clients in the Netherlands are served by CFD providers with their registered office in the Netherlands and by providers with their registered office in another Member State, such as Cyprus, Denmark, Luxembourg and the United Kingdom.

33) Pursuant to the ESMA Decision and the extensions thereof, CFD providers must always display risk warnings in the manner set out in Article 2, fifth paragraph, of the present decision at the moment of the adoption of the present decision. Part of the risk warnings includes the indication of the percentage of retail clients[16] who sustained a loss in the previous 12 months trading in CFDs with the relevant provider. The AFM has established on the basis of the risk warning of CFD providers who focus (in part) on retail clients in the Netherlands that the average indicated loss percentage amounts to 76%. [17]

34) A stark picture emerges of the significant investor protection concern raised by the offer of these CFDs to retail clients. The abovementioned (loss) figures confirm the existence of a significant cause for concern about investor protection where CFDs are concerned.

3.1.4 The type of clients involved (Article 21, second paragraph, under (c), Delegated Regulation)

35) CFDs are marketed, distributed or sold to retail clients on a large scale. The financial threshold for purchasing CFDs is low. Clients can already purchase CFDs if they deposit a small amount of money (€100 for example). This means that CFDs are accessible to a wide public.

[14] The total number of clients with an account with CFD providers is higher because this also includes clients who did not trade actively in the period observed.
[15] The AFM holds data in respect of part of the providers that describe only part of 2017. The estimate was performed by extrapolating the data.
[16] The risk warning itself mentions retail investor.
[17] Reference date 28 January 2019.

36) Retail clients with CFDs invest indirectly in the underlying value. This means that CFDs allow a wider public to trade in the underlying values, which would otherwise not have been available to the public. The leverage of CFDs also enables retail clients to trade larger positions in the underlying value, which would not have been possible for the retail client in question without the leverage.

37) In addition, CFDs are often offered via platforms that can reach a wide public (such as internet search engines, social media platforms or large football clubs). This contrasts sharply with the complexity of CFDs, which, as considered above in 3.1.1, is very difficult to understand for retail clients. The fact that CFDs are mainly sold without advice or portfolio management means that providers of CFDs have limited insight into the personal situation or core objectives of the client. This contributes to the significant risk that CFDs wind up with a wide audience rather than with a specifically-described target group. The evidence of losses sustained by retail clients mentioned in 3.1.3 therefore confirms to the AFM that offering CFDs to retail clients without restriction involves a significant cause for concern about investor protection.

3.1.5 Marketing and distribution activities in relation to CFDs (Article 21, second paragraph, under (j), Delegated Regulation)

38) Although CFDs are complex products, they are offered to retail clients most commonly via electronic trading platforms, without the provision of investment advice or portfolio management. An assessment of appropriateness is required in such cases pursuant to Article 4:24 Wft. Providers are obliged to warn clients if they assess that the service or product is not suitable. However, this assessment does not prevent CFDs, without applying restrictions, from winding up with clients to whom they are patently unsuited.

39) Similarly to NCAs in other Member States, the AFM has observed aggressive marketing practices as well as misleading marketing communications in this sector of the market. They include, for example, the use of sponsorship arrangements or affiliations with major sports teams, which give the misleading impression that complex and speculative products such as CFDs are suitable for the retail mass market by promoting general brand name awareness. Furthermore, they also include the use of misleading statements such as 'Trading has never been so easy', 'Start your career as a trader right now', 'Earn GBP 13,000 in 24 Hours! Get started'.

40) Part of the CFD providers with retail clients in the Netherlands have their registered office in the United Kingdom. The Financial Conduct Authority (**FCA**), which is the NCA in the United Kingdom, observed repeated failings by the approach of CFD providers to completing the appropriateness assessment, including inadequacies in the assessment itself, inadequate risk warnings to retail clients who failed the appropriateness assessments and lack of establishment of a process to assess whether clients who fail the appropriateness assessment, but who nonetheless wish to trade CFDs, should be allowed to proceed with CFD transactions. Revisiting this issue in late 2016, the FCA found that a significant number of firms had failed to address these failings following the previous feedback provided to them.

41) Furthermore, the AFM and other NCAs have voiced concerns about CFD providers' compliance with their obligations to give clients clear and not misleading information, and act in the best

interests of clients. NCAs have also voiced concerns regarding the inadequate performance of appropriateness tests in practice and inadequate warnings to clients when they fail the appropriateness test.

42) Examples of these bad practices are described in and gave rise to ESMA's Questions and Answers relating to the provision of CFDs and other speculative products to retail clients under MiFID. In the context of the development of the CFD Q&As, some NCAs have reported to ESMA that CFD providers often fail to adequately disclose the risks of these products. In particular, some NCAs found that CFD providers did not adequately describe the potential for rapid losses that could exceed their invested funds.

43) Also in this context, some NCAs have also raised concerns about the 'churning' nature of some CFD providers' business models. Because the average life span of a client account can be relatively short, this can place a certain pressure on providers to maintain a steady stream of new clients, which could incentivise providers to adopt aggressive marketing and sales techniques that are not in the retail client's best interests.

44) A common feature of marketing and sales techniques adopted by the CFD industry has been the offer of trading (monetary and non-monetary) benefits, such as bonuses to attract and encourage retail clients to invest in CFDs, the offer of gifts (for example holidays, cars, electronic goods), trading tutorials or reduced costs (for example spread or fees).

45) Bonuses and other trading benefits can act as a distraction from the high-risk nature of the product. They are typically targeted to attract retail clients and incentivise trading. Retail clients might consider these promotions a central product feature to the point where they might fail to properly assess the level of risks associated with the product.

46) Furthermore, such trading benefits to open CFD trading accounts often require clients to pay funds to the provider and conduct a specified number of trades over a specified period of time. Given that the evidence demonstrates that the majority of retail clients lose money trading CFDs, this often means that clients lose more money from trading CFDs more frequently than they otherwise would have without receiving a bonus offer.

47) Supervisory work by several NCAs has discovered that the terms and conditions on promotional offers are often misleading and that many clients were unaware of the conditions to access the benefits/bonuses offered. Finally, a number of clients reported difficulties in withdrawing funds when trying to use such bonuses.

48) In addition to the factors outlined above, many NCAs, including the AFM, observe that distribution models observed in this sector of the market bear certain conflicts of interest. The pressure to maintain a pipeline of new clients increases the potential for conflicts of interest to occur. Conflicts of interest have and may arise from the fact that some CFD providers are counterparties to clients' trades without hedging their exposure, therefore placing their interests in direct conflict with that of their clients. For these providers there is a greater risk and incentive to manipulate or use less transparent reference prices, or to pursue other questionable practices such as cancelling profitable trades on spurious pretexts. There is also a risk that providers may seek to exploit asymmetric slippage (for example pass on any loss as a result of slippage to the

client, while retaining any profit obtained as a result of slippage). Providers may purposefully delay the time between quotes and execution of CFD trades to further exploit this practice. The AFM and other NCAs have also identified practices whereby CFD providers apply an asymmetrical or inconsistent mark up to core spreads.

49) The marketing and distribution practices associated with CFDs described above confirms the existence of a significant investor protection concern in respect of these CFDs.

3.2 Applicable requirements do not address the investor protection concern (Article 42, second paragraph under b, MiFIR)

50) As required under Article 42, paragraph 2, under b, MiFIR, the AFM has considered whether existing regulatory requirements in the Union that are applicable to the provision of investment services pertaining to CFDs avert the above concern and whether it would not be better to deal with the issue on the basis of improved supervision or enforcement of the existing requirements. The relevant applicable requirements when offering financial instruments such as CFDs are laid down in among other places MiFID II and the implementation thereof in the Wft and the Decree on Conduct of Business Supervision of Financial Undertakings under the Wft (**BGfo**) and Delegated Regulation (**MiFID II Delegated Regulation**).[18] In this decision, the AFM will discuss in particular several statutory requirements that could address the investor protection concern. The AFM concludes that in the present case, investor protection concerns cannot be removed with improved supervision and enforcement of these requirements because of the risks identified above and due to the detrimental effect of CFDs for retail clients.

51) The AFM is of the opinion that the following requirements in particular are relevant to the present measure:

- the requirement to provide appropriate information to clients in accordance with Articles 4:19, 4:20 and 4:22 Wft, and further elaboration thereof in Article 58 BGfo,[19] as well as the requirements included in Chapter III, Part 1 of the MiFID II Delegated Regulation and the requirements that investors are provided with information in accordance with Articles 5 up to and including 14 of Regulation (EU) No. (PRIIPS Regulation);
- the suitability and appropriateness requirements as laid down in Articles 4:23 and 4:24 Wft;[20]
- the best execution requirements in accordance with Articles 4:90a et seq. Wft[21]; and
- the product governance requirements in accordance with Articles 4:14 and 4:90 Wft and Articles 32 up to and including 32d BGfo.[22]

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[18] Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive, OJ L 87, pp. 1-83.
[19] Article 24, third, fourth and fifth paragraph, MiFID II.
[20] Article 25, second, third, fourth and sixth paragraph, MiFID II.
[21] Article 27 MiFID II.
[22] Article 16, third paragraph, and Article 24, second paragraph, MiFID II and Chapter III of Commission Delegated Directive (EU) 2017/593 of 7 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits.

52) This decision discusses in particular the requirements included in the Wft and the BGfo. These requirements arise from MiFID II and equivalent requirements apply in all other Member States as well in view of the maximum harmonisation intended by means of MiFID II. Where the AFM refers to existing requirements in the Wft and the BGfo that would not provide a better solution to the matter, the AFM also aims to refer to the requirements arising from MiFID II and the national implementation in other Member States as these apply to investment firms with their registered office in those other Member States or investment firms with their registered office in the Netherlands that offer CFDs via a branch or the freedom to provide services (European Passport).

3.2.1 Provision of information

53) The Wft imposes requirements with respect to the provision of information to (potential) clients. Those requirements concern among other things the provision of correct, clear and non-misleading information[23] and the (timely) provision of certain information.[24] That information includes in particular appropriate information and warnings about the risks inherent in investment in financial instruments and whether the financial instrument is intended for retail clients or professional investors. Investment firms are also obliged to provide their clients with information concerning all costs and additional fees related to the investment services and the financial instruments.

54) There are also requirements with respect to the provision of information of investors on the basis of the **PRIIPs Regulation**.[25] The PRIIPs Regulation imposed uniform rules regarding the shape and content of the key information document to be drawn up by PRIIP[26] developers as well as with respect to the provision of the key information document to retail clients in order to enable them to understand and compare the key characteristics and risks of a PRIIP. Specifically, Article 5 of the PRIIPs Regulation, as implemented further by Commission Delegated Regulation (EU) 2017/653, sets out a methodology for the presentation of the summary risk indicator and the related explanation, for example concerning the question whether the retail client could lose the entire amount in invested capital or whether they have to assume further financial obligations.

55) The AFM is of the opinion that compliance with the requirements concerning the provision of information cannot address the significant cause for investor protection concern. Firstly, the provision of information does not have an influence on the specific characteristics or components of CFDs as described in paragraph 3.1.2. In particular, improving information does not reduce the significant risk of loss or the negative expected value of CFDs. Secondly, the complexity of CFDs as described in paragraph 3.1.1 is such that even if the legal requirements to provide information are satisfied, the products will still be difficult to understand for retail clients.

[23] Section 4:19, first subsection, Wft.
[24] Section 4:20 Wft in conjunction with Section 58 Bgfo and Articles 44 up to and including 51 of the MiFID II Delegated Regulation.
[25] Regulation (EU) No. 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs).
[26] Packaged retail and insurance-based investment product, as defined in Article 4, third paragraph, PRIIPs Regulation.

3.2.2 Assessment of the suitability and appropriateness of the investment service and product

56) The requirements with respect to the suitability of the financial instrument as referred to in Article 4:23 Wft were further strengthened under MiFID II with the obligation to provide a suitability report to the retail client as well as a further description of the suitability assessment. The objectives of the suitability assessment (considering products against clients' knowledge and experience, financial situation, risk tolerance and investment objectives) are substantially unchanged compared to the rules that applied under MiFID I[27]. The requirement to obtain sufficient relevant information and assess the suitability of the investment service or financial instrument to be provided is elaborated further in Articles 54 and 55 of the MiFID II Delegated Regulation. Specifically, Article 4:23, first paragraph, under a, Wft requires investment firms to obtain the necessary information regarding the client's or potential client's knowledge or experience in the investment field relevant inter alia to the specific type of product, the client's or potential client's financial situation including their ability to bear losses, and their investment objectives including their risk tolerance so as to enable the CFD provider to recommend the client or potential client financial products that are suitable for them and are in accordance with their risk tolerance and ability to bear losses.

57) However, the suitability requirements are only applicable to the provision of investment advice and portfolio management. They are usually irrelevant in relation to the marketing, distribution or sale of CFDs, which mostly occurs via electronic platforms, without the provision of investment advice or portfolio management. These requirements are therefore insufficient to remove the significant cause for investor protection concern.

58) In addition, implementation of MiFID II has also led to strengthening of the suitability requirements, in particular by reducing the number of products designated as non-complex as well as the scope for execution only services. Investment firms are obliged on the basis of Article 4:24, first paragraph, Wft to obtain information from their (potential) clients concerning their knowledge and experience in the investment field relevant inter alia to the specific type of product that is offered or desired, so that the provider is able to assess whether that product is suitable for the client or potential client. The providers warns the client or potential client if the provider considers that the product is not suitable for the client or potential client.

59) CFDs are complex financial products and are therefore subject to the appropriateness test in accordance with Article 4:24 first paragraph Wft. However, this was already the case under MiFID I, which provided for a suitability assessment that does not differ essentially from the assessment under MiFID II. Failure to comply correctly with the requirements pertaining to suitability does not contribute or contributes to a very limited extent to the criteria and factors described in paragraphs 3.1.1 up to and including 3.1.6 that give cause for concern about investor protection. What is more, requirements with respect to suitability cannot prevent a retail client from trading in CFDs even if non-suitability has been demonstrated. It is therefore not probable that improved supervision and enforcement of compliance with the requirements pertaining to suitability is able to remove the significant cause for concern about investor protection.

[27]Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 3/22/EEC (OJEU L 145 of 30.4, 2004, page 1).

3.2.3 Best execution requirements

60) Most of the relevant rules with respect to best execution as referred to in Article 4:90a et seq. of the Wft already existed under MiFID I. Those rules were strengthened under MiFID II. For example, market participants must publish additional information and in particular investment firms are required to disclose the top five venues where they executed client orders and the outcomes achieved when executing those orders.[28]

61) Best execution requirements clearly do not have an impact on the degree of complexity or the characteristics and components of the product itself. This means that supervision or enforcement of these requirements cannot lead to a change in the factors and criteria set out in paragraphs 3.1.1 and 3.1.2. Supervision and enforcement of these requirements do not have an impact either on the factors and criteria set out in paragraphs 3.1.3 up to and including 3.1.6. Supervision and enforcement of the abovementioned criteria therefore cannot remove the significant cause for concern regarding investor protection that has been identified.

3.2.4 Product governance requirements

62) The AFM has investigated the potential consequences of the product governance rules following from Article 4:14 Wft, Article 4:90 Wft and Articles 32 up to and including 32d BGfo. These rules require providers manufacturing financial instruments (including therefore CFDs) for sale to clients to ensure that the products are designed to meet the needs of an identified target market of end clients within the relevant category of clients; that the strategy for distribution of the products is compatible with the identified target market; and that the providers take reasonable steps to ensure that the financial instruments are distributed to the identified target market and periodically review the identification of the target market and the performance of the product. CFD providers shall understand the financial instruments they offer or recommend and also assess the compatibility of the instrument with the needs of the client to whom it provides investment services. Also taking into account the identified target market of end clients, and ensure that financial instruments are offered or recommended only when it is in the interest of the client. Furthermore, CFDs providers that distribute financial instruments not manufactured by them shall have appropriate arrangements in place to obtain and understand the relevant information concerning the product approval process, including the identified target market and the characteristics of the product. CFDs providers distributing financial instruments manufactured by providers not subject to the product governance requirements in MiFID II or by third-country providers shall also have appropriate arrangements to obtain sufficient information about the financial instruments.

63) The AFM notes that the product governance requirements arise from MiFID II. On 2 June 2017, ESMA published the ‘Guidelines on MiFID II product governance requirements’ in which guidance is provided to manufacturers and developers for the assessment of the target market.

64) The purpose of the product governance requirements is to narrow down the type of clients (that is, the target market) for which financial instruments would be appropriate and to which they

[28] See Section 4:90b, third paragraph, Wft.

should therefore be distributed. If the financial instruments are not or no longer appropriate for the need, characteristics and objectives of the target group, or if the financial instruments are offered outside the identified target group, the provider will be obliged to implement appropriate measures. An appropriate measure may be adjustment of the target group, the manner of distribution and/or the product.

65) Product governance requirements have applied to developers and distributors of financial instruments since 3 January 2018. The AFM did not observe a material change in the manner in which investment firms offer CFDs to retail clients following the entry into force of the product governance requirements. The AFM did not observe changes in the offer of CFDs that contribute to the removal of the significant cause for concern regarding investor protection until after the ESMA Decision entered into force. The AFM considered whether improved supervision and enforcement of the product governance requirements could address the significant cause for concern regarding investor protection caused by CFDs. The AFM concludes that such an approach is not effective and therefore insufficient to address the problem. The AFM explains this as follows.

66) Concern about investor protection pertains not only to an individual provider of CFDs, but constitutes a market-wide issue. An enforcement process on the basis of product governance requirements is complex and intensive by its nature. Enforcement at all CFDs providers would therefore be disproportionately burdensome for both the providers concerned and the responsible NCAs. What is more, enforcement on the basis of product governance requirements cannot prevent newly-developed CFDs from creating significant cause for concern about investor protection.

3.3 The decision is proportionate (Article 42, second paragraph, under c, MiFIR)

67) In view of the extent and nature of the identified significant cause for concern about investor protection, the AFM considers it necessary and proportionate to restrict the marketing, distribution and sale of CFDs to retail clients.

68) The restrictions of Article 2, first, second and third paragraph, of this decision are intended to limit the risks of trading in CFDs. The restrictions of Article 2, fourth paragraph, aim to improve the provision of information when CFDs are offered. The restrictions of Article 2, fifth paragraph, are intended to protect retail clients against undesirable incentives to trade in CFDs. These restrictions take account of the nature of the identified risk as well as the knowledge level and the expected impact on retail clients who trade in CFDs. The AFM notes in this connection that the restrictions do not lead to retail clients being unable to trade in CFDs. Nor do the restrictions have an impact of the possibility of retail clients to close positions in CFD they already hold.

69) The AFM applies the restrictions in the present decision as those that apply in the ESMA Decision. The AFM's decision to align fully with the restrictions in the ESMA Decision is based on the following.

70) Firstly, the AFM endorses ESMA's assumptions and conclusion that form the basis for the restrictions in the ESMA Decision. The AFM evaluated ESMA data analyses with respect to CFDs

including the simulation model[29] that was applied and the responses to the Call for Evidence[30] reported in the ESMA Decision. Secondly, last year the CFD providers already adjusted their business operations in line with the ESMA Decision. Applying in the present decision the same restrictions as those included in the ESMA Decision instead of deviating restrictions prevents CFD providers from having to adjust their business operations again. Thirdly, offering CFDs often involves cross-border services. Several NCAs have already imposed their own national measures that are in line with the ESMA Decision. A uniform set of restrictions within the EU is desirable in view of the cross-border services provided by CFD providers. Applying the same restrictions as those included in the ESMA Decision contributes to this aim.

71) These restrictions counter the significant cause for concern regarding investor protection by realising a suitable and uniform level of protection for retail clients who are served by providers of CFDs in or from the Netherlands. The AFM is of the opinion that the current restrictions are sufficient to counter the significant cause for concern regarding investor protection. The AFM will continue to monitor developments and reconsider, expand or otherwise change the present decision in the future if necessary.

72) The main advantages of the present AFM measure are the following:

i. reduction of the miss-selling of CFDs and its related financial consequences. This is an important advantage, both for the retail client and for the financial markets as a whole; and

ii. restoration of retail clients' confidence in financial markets, including confidence in the providers in the financial sector whose reputation may have suffered under the problems experienced by investors.

73) The AFM will first explain the limitations of the present decision. The AFM will then explain why the decision as a whole is proportionate.

3.3.1 Initial margin protection

74) The AFM considers it necessary to restrict the marketing, distribution or sale of CFDs to retail clients by the application of certain specific leverage limits depending on the nature of the underlying value.

75) The introduction of these leverage limits will protect clients by requiring them to pay a minimum initial margin in order to enter into a CFD. This requirement is known as ‘initial margin protection’. This will limit the client's notional investment exposure in relation to the amount of money invested. This limitation of the leverage limits contributes to retail client protection and to addressing the investor protection concern. The AFM explains this as follows.

76) Firstly, a higher leverage leads to higher sensitivity of CFDs to price changes of the underlying value and this to a larger risk of the CFDs. Limiting the leverage limits this risk. Secondly, a higher leverage leads to a higher notional exposure. The costs of a CFD increase in line with the notional exposure and as the costs increase, so does the probability of a loss with a CFD. The leverage

[29] See paragraph 3.3.1 of this decision.
[30] See recitals 92 up to and including 104 of the ESMA Decision.

limits limit the increase of the abovementioned loss probability. Thirdly, a higher leverage leads to a greater probability that the initial margin is no longer sufficient, which means that the position is closed by the provider and at a loss. The leverage limits reduce the probability that a position will be closed by the provider at a loss.

77) For the purpose of the ESMA Decision, ESMA determined for various categories of underlying value the initial margin protection according to the volatility of that underlying value on the basis of a simulation model to assess the likelihood of a client losing 50% of their initial investment over an appropriate holding period. Specifically, ESMA undertook a quantitative simulation of the distribution of returns an investor in a single CFD might expect to receive at different leverage levels. The starting point of the simulation was approximately 10 years of daily market price data (in most cases) for various underlying values that are commonly used in CFDs sold to retail clients. For the purpose of the analysis, ESMA considered a CFD that is automatically closed out if the margin reaches 50% of its initial value. The simulated probability with which close-out occurs depends on (and increases in) the given leverage. A metric examined was the probability of (automatic) close-out as a function of leverage. This metric allows for leverage limits to be set according to a model that is expected to address detriment on a consistent basis across different underlying value types.

78) The AFM agrees with ESMA that, given the retail nature of investors and statistics on the distributions of CFD holding periods (using data collected by NCAs) it was appropriate to set initial margin protection by assuming retail clients hold an asset for at least one day. To provide a consistent reference point, ESMA then simulated what leverage would lead to margin close-out with a 5% probability, for different underlying assets. The range of results within each asset class then informed the selection of leverage limits. In most cases, the limits were set conservatively towards the lower end of the range. Consideration was given to how widely traded different assets are. For example, among CFDs on commodities, oil and gold are both commonly traded by retail clients, but simulations indicate that the leverage implying a 5 % probability of margin close-out for CFDs in gold is around twice that of CFDs in oil. The leverage limit for CFDs in gold is accordingly different to that for those in oil and other commodities. Determining initial margin protection in this way, in particular through simulated positions lasting at least one day, provides a consistent and necessary level of protection for retail clients who may not actively monitor their position over the course of a trading day or may not be able to assess the need for quick reactions in light of the volatility of the underlying market. In the case of CFDs on equities, data suggest that holdings are typically longer than for other assets, and consideration was given to holding periods of up to five days.

79) The ESMA Decision furthermore shows that ESMA considered alternative approaches to the calibration of the initial margin protection. For example, an alternative would be to set a single leverage limit for all CFDs irrespective of their underlying value. However, the AFM agrees with ESMA that it would be appropriate to distinguish between different underlying value types given differences in historic price volatility between different classes of underlying value, in addition to differences in typical fee structures within the current CFD firm population and typical client behaviour.

80) The AFM therefore applies the same leverage limits as those that are applied in the ESMA Decision. Only cash payments made by or on behalf of the retail client are taken into account for

the determination of the initial margin and therefore the leverage. Payment that is financed on the basis of credit provided to the retail client by the CFD provider, irrespective of whether the credit is hedged by collateral, therefore does not apply as payment for the determination of the initial margin. In the event the CFD offers exposure to the underlying value by means of another derivative, one as it were 'sees through the other derivative' for the determination of the initial margin. For example, 3.33% of the notional value of the CFD applies as the initial margin in case of a CFD with a future in respect of the USD/EUR currency pair as underlying value, which is the percentage that applies to the USD/EUR currency pair as underlying value.

3.3.2 Margin close-out protection

81) Another measure to protect retail clients is the margin close-out protection. This measure complements the introduction of initial margin protection and mitigates the risk of retail clients losing significant funds in excess of the funds they have invested in a CFD, under normal market circumstances.

82) The provision of a margin close-out protection and the standardisation of the percentage at which CFD providers are required to close-out a client's open CFD (at 50% of the initial required margin) is also designed to address the inconsistent application of margin close-out practices by CFD providers. By allowing clients to erode their margin close to zero, providers are placing clients at risk of losing more than their deposited funds, particularly during a gapping event. Conversely, a too high level of margin close-out would expose clients to be frequently closed out which might not be in their interest. The AFM agrees with ESMA in the ESMA Decision that the 50% threshold set out in ESMA's measure mitigates the risk of substantial loss by retail clients and is therefore proportionate.

83) ESMA performed for the purpose of the formation of the ESMA Decision an analysis of the expected impact on investors of a margin close-out rule per position (in which connection a CFD is closed as soon as its value drops below 50% of the value of the initial margin) versus a close-out per CFD account (in which connection a CFD is closed as soon as the value of all open CFDs in the account, together with all funds in that account, drops below 50% of the value of the total initial margin for all CFDs that were opened). In particular, it assessed the frequency of close-out and the impact of crystallising client losses for a simulated portfolio of CFD positions under each scenario. This analysis did not estimate precise numerical outcomes, reflecting that there is an extremely large range of different potential portfolios that an investor could hold. Instead, the analysis considered whether either of the two bases would be expected in general to lead to better outcomes for investors. The general conclusion was that the better investor outcome for a position or account basis of margin close-out depends on the price movements of the underlying values of the CFDs in investment portfolios. The reason for this is that following a close-out which would happen on one basis but not the other, the price of an underlying value may recover or may deteriorate.

84) While the difference in outcomes resulting from the per position basis versus the per account basis is expected to be small for many investors (but cannot be precisely quantified in the absence of a representative portfolio), the Call for Evidence responses highlighted additional reasons why an account basis may be better for some investors. Firstly, in allowing gains from

one position to offset losses from another, an account basis supports a diverse portfolio of investments. Secondly, to the extent close-out happens less frequently on an account basis, it reduces the scope for investors to bear costs arising from re-entering positions.

85) Taking into consideration the above ESMA analysis to which the AFM concurs and the responses from the call for evidence, the AFM agrees with ESMA that a standardised margin close-out rule per account basis at 50% of the total initial margin protection, as an individual measure to take in addition to the other measures described in this Decision, is more proportionate as a minimum protection to be applied. In particular, this rule should provide for close-out of one or more CFDs on terms most favourable to the retail client to ensure that the value of the account does not fall lower than 50 % of the total initial margin protection that was paid to enter into all currently open CFDs at any point in time. The value of the account for these purposes should be determined by the funds in that account together with any unrealised net profits from open CFDs connected to that account. Assets other than CFDs and the funds in the account (other financial instruments for example) are not taken into account in this connection for the purpose of the determination of the value of the account.

86) The margin close-out protection does not prevent a provider from applying a per position close-out rule instead of a per account close-out rule. A provider would do well to establish the impact of the application of both rules next to each other. The AFM also expects that providers communicate about this towards retail clients in a correct, clear and non-misleading manner.

87) A CFD provider could apply the condition that the loss in connection with concluding a CFD can never exceed the investment. The AFM notes that if this is the case, margin close-out protection does not provide additional protection in so far as it concerns preventing losses exceeding the investment. However, if this is the case, margin close-out protection still serves the purpose of countering inconsistent application of margin close by providers.

3.3.3 Negative balance protection

88) The negative balance protection aims at protecting retail clients in exceptional circumstances where there is a price change in the underlying value that is sufficiently large and sudden to prevent the CFD provider from closing out the position as required by the margin close-out protection, such that the client has a negative account value. In other words, large market events can cause gapping, preventing the automatic margin close-out protection from being effective. ESMA reports in the ESMA Decision that a number of NCAs have observed that, following such events, clients have owed considerably more than they invested, ending up with a negative balance on their CFD trading account.

89) The purpose of a negative balance protection is to ensure that an investor's maximum losses from trading CFDs, including all related costs, are limited to the total funds related to trading CFDs that are in the investor's CFD trading account. This should include any funds yet to be paid into that account due to net profits from the closure of open CFDs connected to that account. An investor should not incur any additional liability connected with its trading of CFDs. Other accounts should not be part of the investor's capital at risk. In case a trading account also includes other financial instruments (for example, UCITS or shares), only the funds explicitly

dedicated to CFD trading, and not those dedicated to other financial instruments, are at risk. This means that the provider cannot use the balances of retail clients that have not been designated specifically for the trade in CFDs as negative balance protection.

90) The purpose of the negative balance protection is also to provide a ‘backstop’ in case of extreme market conditions. For the purpose of the formulation of the ESMA Decision, ESMA conducted analysis of the Swiss franc event in January 2015 to consider its direct impact on investors across a number of scenarios. It concerned the following three scenarios:

i. protection against any negative balance on a CFD trading account held by a retail client;
ii. protection against any negative balance on each CFD position held by a retail client; and
iii. no negative balance protection.

91) In assessing these options, ESMA noted in the ESMA Decision that the direct impact on investors resulting from the different options in the case of extreme market events needed to be weighed against the resulting ongoing costs of providing this protection. In particular, CFD providers would face ongoing costs attributable to additional capital or hedging, as part of their risk management. Some portion of these costs could in turn be passed through to investors themselves in the form of higher spreads or other charges.

92) On the other hand, an important risk of major consumer detriment that arises in the absence of negative balance protection is the potential for an investor to owe money to a firm as a result of extreme market conditions. Such a situation is especially detrimental for investors without considerable liquid wealth. ESMA decided to adopt negative balance protection per CFD trading account as a way to address this source of potential major detriment while minimising associated costs to firms and investors. In particular, ESMA considered that the imposition of a negative balance protection per each CFD would have risked imposing disproportionate costs on investors and firms. If a negative balance protection per position were introduced, firms would be required to forgive any losses by the client in excess of the funds dedicated to that position, including initial margin and any additional margin paid by the client. As negative balance protection would not enable the netting of a significant loss with other positions in a client's portfolio, a per position rule would increase the market risk assumed by firms. This would likely result in an increase of the capital requirements for firms, the costs of which would likely be passed on to retail clients.

93) The AFM agrees with ESMA´s analysis set out above. ESMA also considered in the ESMA Decision the responses to the Call for Evidence and weighed the consequences for providers of providing negative balance protection against the major detriment that may be suffered by retail clients if this protection is not offered. The AFM agrees with ESMA that after weighing the interests, on balance, negative balance protection on an account basis addresses the concern regarding the major detriment that could be experienced by retail clients if this protection does not exist and that negative balance protection should therefore be considered to be proportionate.

3.3.4 Risk warnings

94) Another measure to address risks to retail clients in relation to CFDs is to require the provision of standardised and effective firm specific risk warnings including information on the percentage of

retail client accounts' losses. CFD providers must display the risk warnings in a prominent spot. This means that they are not allowed to place risk warnings behind disclaimers or in locations that require the retail client to make an effort to reach them. The presentation of the risk warning, such as the choice of font, the colour or duration of the display of the risk warning, may not result in the risk warning being unclear or insufficiently legible either. The AFM refers in this connection to the purpose of the risk warning, which is to enable retail clients to take note of the information provided by the risk warning so that they can include the information in making a well-considered decision whether to conclude a CFD or not.

95) As set out above, several NCAs have pointed out the poor quality of risk warnings addressed to clients that were displayed by providers of CFDs prior to the ESMA Decision and reported that CFD providers often fail to clearly indicate the high-risk and complex nature of their products. In particular, these risk warnings often failed to explain clearly that the investor's losses could quickly exceed the amount of their investment or that the message is blurred as a result of the manner in which the warning is shown or by statements concerning potential profit.

96) The firm specific risk warnings introduced in this Decision would provide retail clients with essential information about these particular products, namely the percentage of retail accounts losing money when trading CFDs. ESMA refers in the ESMA Decision to a study that found that a standardised risk warning significantly improved a retail client's understanding of the product, including the possibility of losing more money than they invested and the likelihood of making a profit.[31]

97) A requirement for CFD providers to state the percentage of retail client accounts that are at a loss is designed by the AFM to offset the tendency of CFD providers to highlight the potential profits over losses.

98) Furthermore, the AFM expects the warnings to support retail clients in making an informed decision about whether they wish to proceed with a high-risk product that is more likely to result in a loss than a gain.

99) In order to warn investors of the risk of losses related to investing in CFDs, the AFM agrees with ESMA that each CFD provider should inform their clients of the percentage of its CFD trading accounts of retail clients that lost money over the last 12-month period. To ensure the figure is kept up-to-date, this calculation should be updated on a quarterly basis. The percentage shown should be presented in a simple and clear manner as part of a risk warning in every communication of the provider.

100) In order to determine whether an account lost money, both the realised and unrealised profits or losses have to be taken into account. Realised profits and losses relate to the CFD positions that were closed during the calculation period. Unrealised profits and losses relate to the value of open positions at the end of the calculation period. In order to provide a complete picture of the percentage of accounts that resulted in a profit or loss all costs in relation to the trading of CFDs should be taken into account in the calculation.

[31] See recital 127 of the ESMA Decision.

101) For newly established CFD providers and CFD providers that have not had any open CFD positions in the past 12 months, it is not possible to calculate such a percentage over the last 12 months. This decision prescribes for these firms a standardised risk warning in which reference is made to the percentages found by NCAs in their existing studies (Annex II, Section A, Article 5 of this decision).

102) One risk ESMA, the AFM and other NCAs acknowledge of the firm-specific loss percentages is that these percentages will be used for marketing instead of the original purpose, being the risk warning. For these reasons, NCAs should monitor that investment firms do not use the firm-specific percentages in an inappropriate manner. The AFM will monitor the application of the mandatory risk warnings closely and if necessary change this restriction in the future, for example if it becomes clear that the warning does not have the desired effect in practice.

3.3.5 The prohibition of monetary and non-monetary benefits

103) A final measure to address risks relating to the distribution of CFDs to retail clients is a ban on monetary (for example so called ‘trading bonuses’) and certain types of non-monetary benefits. Financial promotions offering bonuses or other incentives to trade CFDs often distract retail clients from the high-risk nature of CFD products. They draw in retail clients who may not otherwise choose to invest in these products. Such benefits are often contingent on clients depositing money on the account or on executing a certain volume of trades.

104) However, the prohibition of benefits does not cover information and research tools provided to retail clients insofar as they relate to CFDs (excluded non-monetary benefits), as these would help clients' decision-making. The prohibition of benefits does not cover general benefits, such as lower transactions, either, which are not intended to persuade the retail client to trade (more) in CFDs.

3.3.6 The decision as a whole is proportionate

105) The AFM has reached the limits of what is effective as regards the use of non-binding tools, such as public warnings against the risks of trading in CFDs. What is more, the AFM acknowledges in this connection and specifically with respect to product governance that the principles of product governance already formed part of the supervisory culture in the financial sector within the Union before MiFID II entered into effect. The European Supervisory Authorities (‘ESAs’) issued a joint position on ‘Manufacturers’ Product Oversight and Governance Processes' setting out high-level principles applicable to the oversight and governance processes of financial instruments. In February 2014, ESMA issued an opinion on ‘MiFID practices for firms selling complex products’ and, in March 2014, it issued an opinion on ‘Structured Retail Products — Good practices for product governance arrangements".

106) Despite these supervisory principles and the regulatory requirements described in this Decision, the detriment in relation to the marketing, distribution or sale of CFDs to retail clients had continued to develop over the years prior to the entry into effect of the ESMA Decision.

107) The AFM therefore considers that the present measures, which restrict the marketing, distribution or sale to retail clients of all types of CFDs to be appropriate to address risks to investor protection. The present decision in its entirety is necessary and proportionate to address the investor protection concern.

108) It is generally expected that the restrictions will reduce the abnormal and significant losses sustained by retail clients when trading in CFDs and also increase awareness of the risks inherent in these products among this group of clients. The potential consequences for CFD providers mainly consist of the potential reduction in sales from the trade in CFDs (as a result of smaller trading volumes, a lower amount in transactions costs paid by clients and lower losses incurred by clients). The fact that CFD providers have been subject to the restrictions under the ESMA Decision since 1 August 2018 means that the financial consequences cannot be related to the adjustment of the business operations because these adjustments were already implemented as a result of the ESMA Decision.

3.4 Consultation NCAs in other Member States (Article 42, second paragraph, under d, MiFIR)

109) The AFM notified all NCAs of the intention to implement the present decision via ESMA Investor Protection and Intermediaries Standing Committee prior to the adoption of the present decision. No NCA in another Member State responded to the effect that it or its Member State may or will suffer a significant impact from the present decision. For the sake of additional care, the AFM also consulted CySEC and FCA individually and directly, because a relatively large number of investment firms that offer CFDs to retail clients in the Netherlands have their registered office on Cyprus and in the United Kingdom. The present decision therefore may have an impact on CySEC and the FCA due to their responsibility as home country supervisor.

3.5 No discriminatory effect on services and activities provided from another Member State (Article 42, second paragraph, under e, MiFIR)

110) This decision applies to the providers of CFDs with their registered office in the Netherlands and to providers of CFDs with their registered office in another Member State that offer CFDs to Dutch retail clients. Investment firms with their registered office in another Member State that provide investment services in the Netherlands are therefore covered by the scope of application of the present measure as are investment firms with their registered office in the Netherlands. It is therefore not likely that the present decision will have a discriminatory effect on services and activities provided from another Member State.

3.6 Consultation with public bodies competent for the oversight, administration and regulation of physical agricultural markets (Article 42, second paragraph, under f, MiFIR)

111) The proposed measure may be related to agricultural commodities derivatives to a limited extent. The AFM therefore consulted for the sake of additional care with the Ministry of Agriculture, Nature and Food Quality, European Agriculture and Fisheries Policy and Food

Security. This consultation did not lead to insights that would lead to a decision different from the present decision.

4. Notification of NCAs in other Member States and ESMA (Article 42, third paragraph, MiFIR)

112) The AFM notified all NCAs in other Member States and ESMA in writing and in the agreed manner of the particulars referred to in Article 42, third paragraph, MiFIR, on 21 February 2019, which is at least one month before the measure takes effect. ESMA adopted and published an opinion on the ESMA website[32] in accordance with Article 43, second paragraph, MiFIR. The AFM took note of the opinion adopted by ESMA. The AFM concludes that the proposed measure is not contrary to the opinion adopted by ESMA.

5. Publication of the notice of the decision on the website (Article 42, fifth paragraph, MiFIR)

113) The AFM publishes a notice of this decision in the following location: https://www.afm.nl/nl-nl/professionals/onderwerpen/productinterventie. The AFM's measure will enter into effect following publication of the notice of this decision on the AFM website and in the Government Gazette.

114) The AFM sees no reason to determine a transitional period, because restrictions on the marketing, distribution or sale of CFDs to retail clients has been in effect in the EU since 1 August 2018. Market participants therefore do not require time in the shape of a transitional scheme to make the necessary adjustments to their business operations. What is more, the AFM informed the market on 7 March 2019 of its intention to adopt at the national level the restrictions included in the ESMA Decision in the near future.

[32] 'ESMA opinion under Article 43(2) MiFIR (AFM_CFDs)', 2 April 2019, https://www.esma.europa.eu/document/esma-opinion-under-article-432-mifir-afmcfds