



Activities Report

2016

Mission

We protect the integrity of the markets managed by BM&FBOVESPA and the investors who trade on them.

Mandates

- Supervision of market activities (orders and trades) to identify any abnormalities or behavior capable of putting at risk the regular functioning, integrity, transparency and credibility of BM&FBOVESPA's markets
- Inspection and auditing of BM&FBOVESPA's participants to verify compliance with the applicable laws, regulations and rules
- Oversight of BM&FBOVESPA's activities as an issuer of listed securities and operator of securities markets ("self-listing")
- Surveillance of the organization and market oversight activities performed by BM&FBOVESPA (Operations Department)
- Surveillance of BM&FBOVESPA's enforcement of the obligations of listed securities issuers (Issuer Regulation Department)
- Conducting disciplinary administrative proceedings to investigate irregularities, and penalizing offenders
- Managing the Investor Compensation Mechanism (MRP)
- Conducting investigations and ruling on compensation claims filed by investors against the MRP
- Establishing the rules and regulations required for the performance of its activities
- Organizing and offering courses, guidance for BM&FBOVESPA's participants, lectures or training regarding its activities

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Introduction

The evolution of the securities market obliges regulators and self-regulating organizations to continuously update and refine their work methods and techniques of supervision, and at the same time they must interact more with market participants to ensure trading is conducted with integrity and transparency on a market that properly fulfills its intermediation and price formation functions.

In order to guarantee the proper functioning of the markets managed by BM&FBOVESPA, in 2016 BSM introduced significant improvements to its auditing, market supervision and enforcement activities and promoted initiatives to enhance communication and transparency with regulated parties and the public in general.

One of BSM's main tasks is to guide and encourage the creation of a compliance culture and the improvement of internal controls of market participants.

In this respect, we continued to hold orientation and clarification seminars to participants. In a seminar held in the second half of 2016, we discussed issues regarding the role of brokers as gatekeepers who must ensure the integrity of the market and protect investors in the conduct of their activities.

In our operational audits we introduced changes to the classification method to evaluate participants in order to improve incentive mechanisms. In an unprecedented way, BSM submitted the proposed change to the method to public consultation with the purpose of eliciting suggestions from participants.

Also within the scope of our auditing activities, we extended the coverage of our operational audits performed on participants of the markets managed by BM&FBOVESPA and included in our work plan operational audits on custodians, gold depositaries and securities underwriters in view of the regulatory changes promoted by CVM.

The data mining systems used for supervision of the markets managed by BM&FBOVESPA also underwent enhancements that allowed it to obtain more evidence and accurate information to initiate administrative proceedings in cases of irregular practices. It should be noted that in 2016 BSM prepared the first cases in Latin America involving layering and spoofing practices in capital markets.

In enforcement activities BSM also introduced innovations to its procedural regulation, which now provides for two enforcement measures – letter of admonition and letter of recommendation. Both measures do not constitute the imposition of a penalty and will be adopted according to the irregularity on a case-by-case basis.

Through this initiative BSM expects to bring a greater number of enforcement measures to participants of the markets managed by BM&FBOVESPA, allowing it to apply the most appropriate measure to remedy the violation identified in its auditing, supervision and inspection activities.

Improved communication and greater transparency were also addressed by BSM during 2016. BSM's website was redesigned to include new features and functionalities, such as the availability of a procedural research tool

that enables the consultation of data on administrative proceedings and complaints to Investor Compensation Mechanisms.

With the purpose of expanding its scope of activities, BSM submitted to CVM's approval the provision of self-regulation services to third parties in its corporate purpose.

The services that may be provided to third parties are the same as those regularly provided by BSM: (a) analysis, supervision and monitoring of transactions and activities carried out by participants of a given market; (B) auditing participants of these markets in order to verify compliance with the regulatory and operational rules of access and performance of the markets in which they trade; (C) establishing, fact-finding, managing and adjudicating administrative and disciplinary proceedings, in accordance with the BSM Procedural Regulation, to investigate possible violations by participants in the markets in which they trade.

BSM will negotiate on a case-by-case basis the extent of the services to be provided depending on the need of the third-party recipient of the self-regulation services.

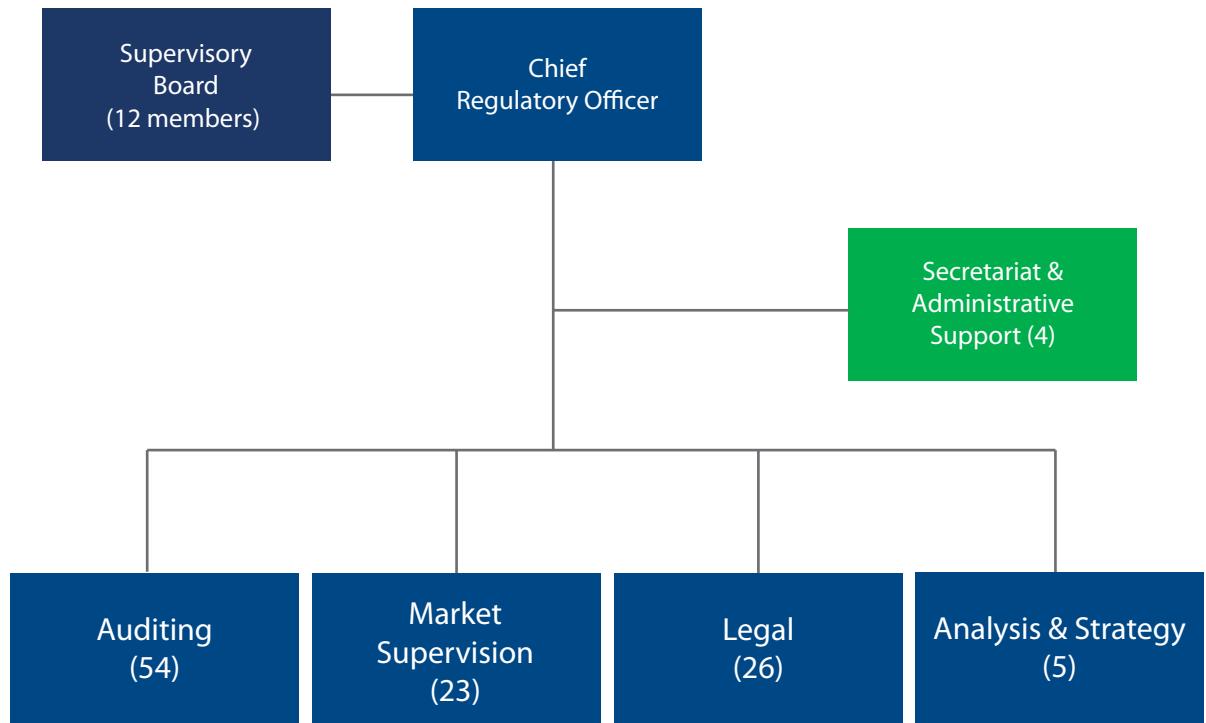
Lastly, it should be noted that BSM's efforts to continuously improve its activities have resulted in an upgrade of its Supervision Risk Classification by CVM as indicated in the CVM Biennial Risk-Based Supervision Plan for 2017-2018¹.

As presented in the Plan, CVM considered for the 2017-2018 biennial a lower probability of occurrence of failures in the supervision of trades carried out in stock exchange and organized OTC markets (risk event No. 1); failures in the supervision of brokers and their agents (including self-employed agents), custodians and underwriters (risk event No. 2); and failures in the supervision and completion of administrative sanctioning proceedings (risk event No. 3). The likelihood of occurrence of failures in handling complaints to the Investor Compensation Mechanism remains low.

In the following pages we present details of the activities carried out by BSM and the main highlights of our activities during 2016.

¹ CVM's biennial plans are available on http://www.cvm.gov.br/menu/acesso_informacao/planos/sbr/sbr.html

Figure 1 – BSM's Organizational Structure



Note: The number of professionals employed by each department is shown in parentheses.



Auditing of Participants

BSM is responsible for direct supervision of BM&FBOVESPA's participants. It discharges this duty by auditing institutions to examine compliance with the applicable laws and regulations.

Audits at BM&FBOVESPA

In accordance with CVM Instruction 461/2007, BSM is responsible for auditing BM&FBOVESPA's Issuer Regulation Department. A report on the 2016 audit will be issued in first-half 2017.

Pre-Operational Audits

To be admitted by BM&FBOVESPA as a participant in a given category and hence have access to its markets, an institution must meet a number of operational, technological and financial requirements.

Compliance with these requirements is verified by BSM in pre-operational audits conducted at BM&FBOVESPA's request. Twelve pre-operational audits were performed in 2016.

Operational Audits – Trading Participants

Operational audits appraise the infrastructure and processes of BM&FBOVESPA's trading participants (PNs), including such items as technology, information security, and business continuity plans, as well as procedures relating to suitability, customer registration, order reception, registration and execution, collateral management, settlement, custody, and risk management. Aspects of investment club management are also verified, as are self-employed investment agents (AAIs) linked to participants.

In 2016 BSM introduced improvements and new tests in the scope of operational audits covering Full Trading Participants (PNPs) and Trading Participants (PNs).

Audits focus on analyzing procedures for supervision of trades and orders with the aim of verifying compliance with CVM Instruction 08/1979 and item 126 of BM&FBOVESPA's Basic Script, as per BM&FBOVESPA Circular Letter 068/2015-DP, which deals with abusive practices in the capital markets such as the creation of artificial demand, supply or pricing, price manipulation, fraudulent transactions, and unfair practices, especially the strategies known as spoofing and layering.

BSM's 2016 work plan also included operational audits of participants that provide services as securities custodians, securities registrars and gold depositories, in compliance with CVM Instructions 542/2013 and 543/2013. The scope of these audits covered participants' processes and internal controls, mainly with reference to CVM Instructions 542/2013 and 543/2013, BM&FBOVESPA's Access Manual as per Circular Letters 040/2014- DP and 046/2014-DP, dealing with conditions for access to BM&FBOVESPA, and BM&FBOVESPA's Standard Rules, as per BM&FBOVESPA Circular Letter 068/2015-DP.

At the end of each year's operational audits, participants are classified according to a score based on percentage non-compliance with the rules and regulations for the organized market in each audited process. The Final Process Score ("Non-Standardized Score") is the sum of the Final Scores for Audited Items in the process. Final Scores for Audited Items are calculated as the product of Control Objective Weight times Audited Item Scores according to a Weights & Audited Items Matrix. Participants are then distributed in bands.

CHANGE TO METHODOLOGY FOR CALCULATING AUDIT SCORES – PUBLIC CONSULTATION

At the end of each annual work plan, the results of all the operational audits are classified in order to create:

- a quantifiable and uniform mechanism for evaluating all participants
- a history of participant performance so that participants can track their evolution over time and compare it with the market, even if requirements change from one year to another
- incentives for participants to pursue better results and win a waiver of operational audits for one or two years according to the results obtained.

In September BSM held a public hearing on a proposal to upgrade the methodology used to classify the results of operational audits of BM&FBOVESPA's participants.

The prime purpose of the public consultation was to collect opinions on the proposed change to the method for calculating the Standardized Final Score in operational audits so as to reflect not just the participant's result compared with other market participants but also the level of process maturity and compliance with normative requirements.

The proposal was presented to participants in a workshop held in September, followed by a period of several weeks for suggestions. BSM received comments from one participant. The outcome of the public consultation and the new version of the methodology were posted on BSM's website in November (as a normative document including the proposed changes).

BSM's Operational Audit Program is annual and covers 100% of BM&FBOVESPA's Full Trading Participants (PNPs, trading participants with direct access to the trading systems) and 100% of its Trading Participants (PNS, trading participants who do not have direct access and trade through PNPs acting as intermediaries).

Chart 1 shows the frequencies of percentage irregularities detected in audits of participants, considering the applicable regulations. The higher the percentage, the worse the participant's position in the audit classification.

Chart 2 shows the distribution of standardized final scores for the audits, classifying participants into four bands by average final score and standard deviation.

Chart 1. Frequency Distribution of Non-standardized Score

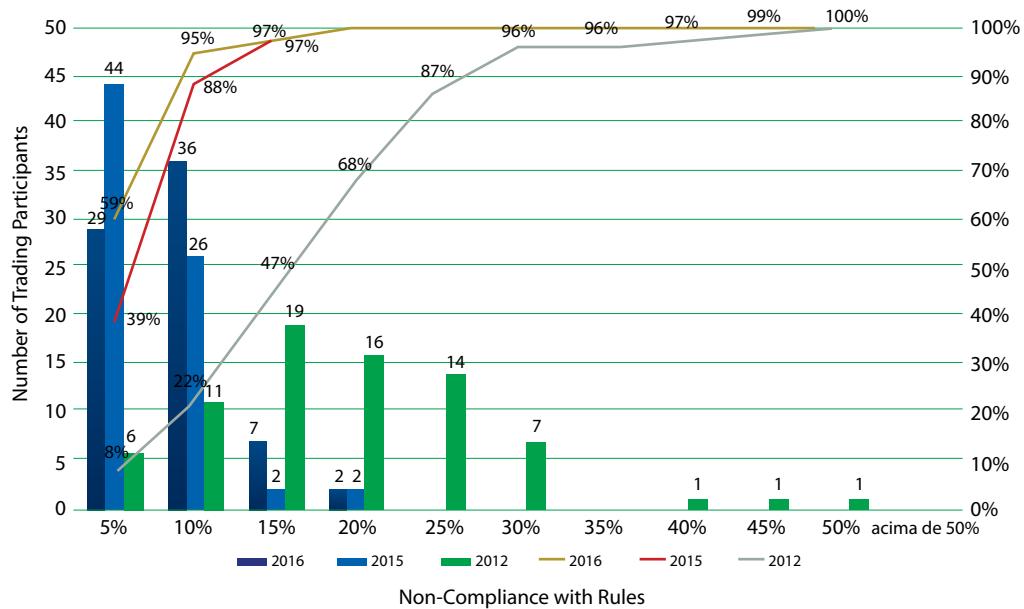


Chart 2. Standardized Final Score - 2016

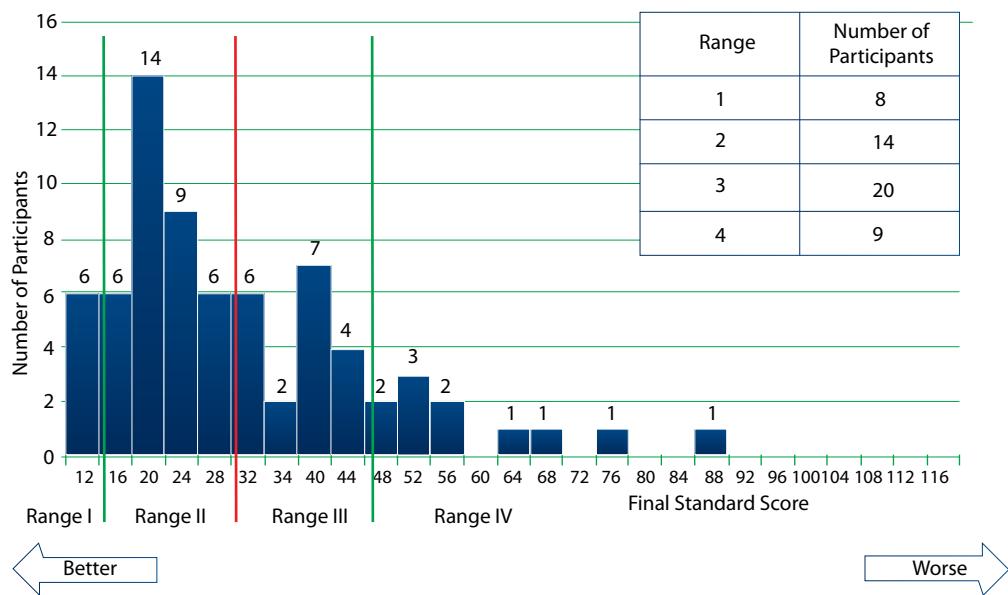


Table 1 presents the distribution of participants by classification band and process. Table 2 shows the limiting scores for each classification band.

Money Laundering Prevention, Supervision of Transactions and Information Security were the least mature processes. The most frequent irregularities found in these processes were deficient monitoring under CVM Instruction 301/1999, article 6 (II, III & VII), the presence of generic users in systems, and staff with access to systems incompatible with their duties.

Table 1

	Range 1	Range 2	Range 3	Range 4
Suitability (554) (Number of Brokerage Houses/Percentage)	(8 / 13%)	(31 / 48%)	(23 / 36%)	(2 / 3%)
Execute Orders (1,402)	(18 / 28%)	(26 / 41%)	(12 / 19%)	(8 / 13%)
Settle Trades (819)	(52 / 81%)	(0 / 0%)	(0 / 0%)	(12 / 19%)
Margin Account (320)	(62 / 97%)	(1 / 2%)	(0 / 0%)	(1 / 2%)
Manage Asset Custody and Positions (514)	(63 / 98%)	(1 / 2%)	(0 / 0%)	(0 / 0%)
Self-Employed Investment Agent (788)	(57 / 89%)	(0 / 0%)	(4 / 6%)	(3 / 5%)
Internal Controls and Professional Certification (799)	(18 / 28%)	(23 / 36%)	(18 / 28%)	(5 / 8%)

LEVEL OF PROCESS MATURITY IN OPERATIONAL AUDITS

Another improvement made with regard to the classification of operational audit results in 2016 was the introduction of the concept of Level of Maturity for audited processes. A mature process is defined as the process with the highest percentage of participants that achieve the Non-Compliance Target among all the participants that have the process. The Non-Compliance Target is percentage non-compliance in relation to the maximum possible for the process, and is set at 3% by BSM.

The Level of Process Maturity is calculated as the ratio of the number of participants who achieve the Non-Compliance Target to the total number of participants that have the process. The higher the maturity, the more the process complies with the applicable rules and regulations. For every process there is a single value of maturity.

Table a and Figure b below present the most important processes and their respective maturity levels.

Participants in Band 1 are granted a one-year audit waiver. In 2016, audits were waived for six participants owing to the results they had obtained in the previous year's operational audit. The other 63 active participants underwent operational audits. Field work in all these institutions was completed on December 23, 2016.

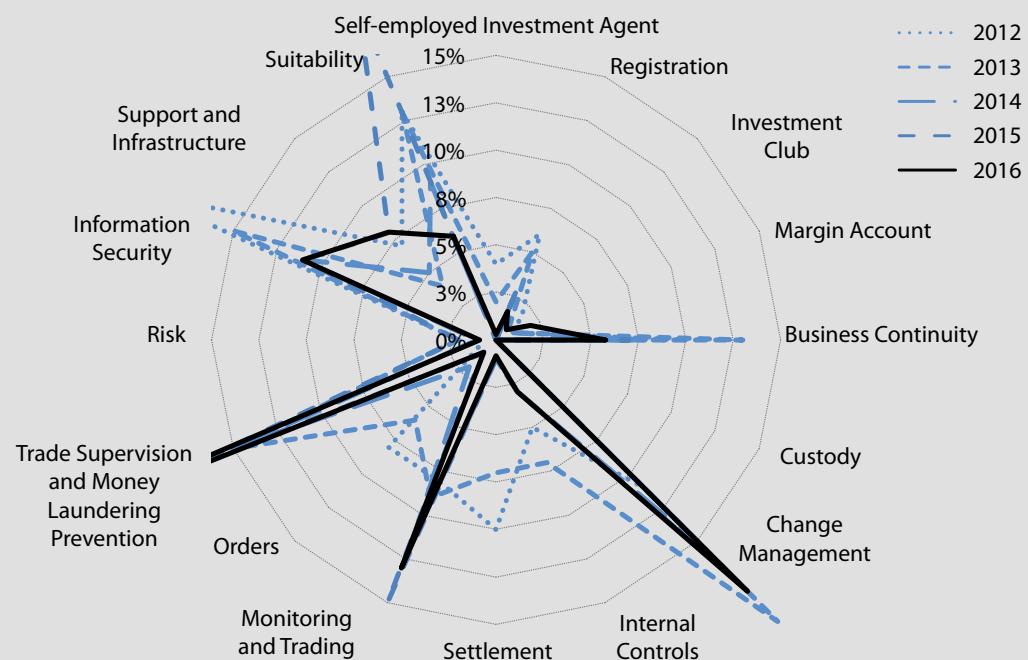
Table a

Process	Maturity Level %
Manage Asset Custody and Positions	100.00%
Self-Employed Investment Agent	97.14%
Investment Club	94.73%
Manage Risk	92.18%
Execute Orders	90.62%
Margin Account	88.88%
Settle Trades	82.81%
Register Customers	78.12%
Business Continuity	68.75%
Internal Controls and Professional Certification	64.06%
Suitability	43.54%
Change Management	40.62%
IT Infrastructure Monitoring and Operation	39.06%
Infrastructure Support	37.50%
Information Security	9.37%
Trade Supervision and Money Laundering Prevention	7.81%

Table 2

	Highest Score 2016	Lowest Score 2016	Average Scores 2016	Average Score 2015	Range 1	Range 2	Range 3	Range 4
Suitability (554) (Number of Brokerage Houses/ Percentage)	51.05%	0.00%	5.89%	18.87%	0	0,01% a 5,89%	5,90% a 13,23%	13,24% a 100%
Execute Orders (1.402)	4.88%	0.00%	0.92%	1.32%	0	0,01% a 0,92%	0,93% a 2,14%	2,15% a 100%
Settle Trades (819)	8.24%	0.00%	0.84%	0.94%	0	0,01% a 0,84%	0,85% a 2,71%	2,72% a 100%
Margin Account (320)	16.14%	0	1.98%	2.05%	0	0,01% a 1,98%	1,99% a 7,01%	7,02% a 100%
Manage Asset Custody and Positions (514)	0.96%	0.00%	0.04%	0.07%	0	0,14% a 100%	-	-
Self-Employed Investment Agent (788)	3.91%	0.00%	0.27%	0.20%	0	0,01% a 0,27%	0,28% a 1,00%	1,01% a 100%
Internal Controls and Professional Certification (799)	21.55%	0.00%	2.94%	3.45%	0	0,01% a 2,94%	2,95% a 6,58%	6,59% a 100%

Chart b



As mentioned above, operational audits include inspection of self-employed investment agents (AIs) linked to participants. Among other items, inspections entail verification of these representatives' physical and technological structures, as well as their procedures. BSM audited 349 AIs in 2016.

Indirect audits

Indirect auditing combines information obtained from a range of sources and treated with statistical software. This activity, considered a complement to direct audits, assesses participants' compliance with the applicable rules and regulations by analyzing the entire universe of information instead of samples only.

The following items were indirectly audited in 2016:

- Compliance with the minimum requirements regarding financial situation and net worth established by BM&FBOVESPA's rules
- Related-party transactions and own-account transactions by the institution
- Analysis of investors' and participants' proprietary current accounts to detect irregular extension of credit to customers
- Investor portfolio turnover and churning²
- Verification of compliance by participants with their own operational rules and parameters
- Certification of professionals.

DMA auditing

DMA stands for Direct Market Access, which occurs when the investor accesses BM&FBOVESPA's trading system directly by means of an automated connection. Four categories of DMA are currently available for direct access to BM&FBOVESPA.³

Regardless of the DMA model used, an investor can only access the Exchange through a participant, which is responsible for monitoring customers' trades and setting trading limits for them.

To preserve market integrity, it is important for participants to have adequate systems for controlling pre-trading risk (systems that check whether orders sent and positions held by customers comply with certain prerequisites).

BSM is responsible for auditing these pretrading risk control tools when requested to do so by BM&FBOVESPA. Six were audited in 2016.

² Churning is excessive trading by a broker in a customer's account, largely to generate commissions.

³ Details of BM&FBOVESPA's Direct Market Access (DMA) models can be obtained from BM&FBOVESPA's website (Services / Trading Solutions / Direct Market Access (DMA)).

MRP audits

MRP audits are performed to clarify technical issues in proceedings relating to claims against the Investor Compensation Mechanism (MRP).⁴

In 2016, BSM produced 767 audit reports for the fact-finding and investigative stage of MRP proceedings. Growth in MRP auditing reflected the number of claims received following the extrajudicial liquidation of TOV CTVM.

Other audits

BSM also performs special audits requested by the Chief Regulatory Officer, in response to specific factors such as issues identified in audits performed, complaints, or orders from CVM, the Central Bank of Brazil or BM&FBOVES-PA's CEO. In 2016, BSM performed 12 special audits.

BSM offers a channel on its website for complaints by the general public. Its aim is to foster communication between the public and BSM.

Tables 3 and 4 present the numbers and types of audits performed by BSM in 2016 and interaction with the market by the auditing team.

Table 3: Audits performed in 2016

Type of audit	No.
Pre-operational	12
Operational – Trading Participants	66
Operational – Depositary / Custodian / Underwriter Participants	18
DMA (Direct Market Access)	6
MRP (Investor Compensation Mechanism)	767
Autonomous Investment Agents (AAI)	349
Specific Audits	14
Total audits	1,232

⁴ For more information about the MRP, see the relevant section of this Report (p. 30).

Table 4: Interactions with the Market

Activity	Total
Meeting with Market Participants for technical guidance	99
Meeting with BM&FBOVESPA	23
Training for CVM	2
Guidance to Vendors	2

In accordance with due diligence best practice, in December BSM consulted CVM for guidance on interpreting articles 1 and 2 of CVM Instruction 539/2013, with regard to the definition of customers' investment profiles, product recommendations, performance of transactions, and provision of services based on suitability. BSM's query and CVM's reply are available on BSM's institutional website.

BSM also participated in a review of BM&FBOVESPA's rules and regulations, especially a discussion of the accreditation of trading area professionals, the creation of bank order conveyors, which resulted in Circular Letter 030/2016-DP, and the certification of professionals.



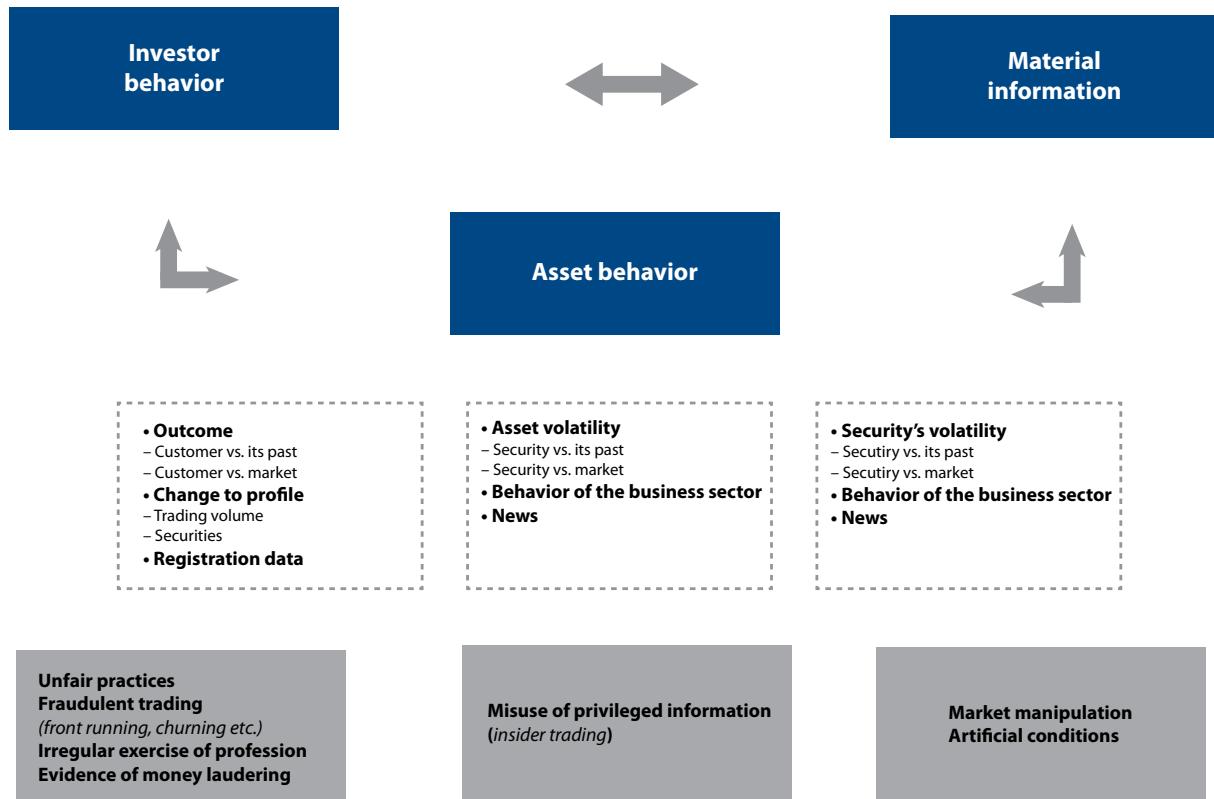
Market Supervision

BSM's market supervision activities consist of monitoring the markets to detect deviations that may relate to the execution of irregular transactions.

The aim of these activities is to identify practices such as market manipulation, insider trading, creation of artificial demand, supply or pricing, unfair practices, and the irregular exercise of activities in the securities markets.

The figure below presents BSM's market supervision procedures in summarized form.

Figure 2. Dimensions of market supervision

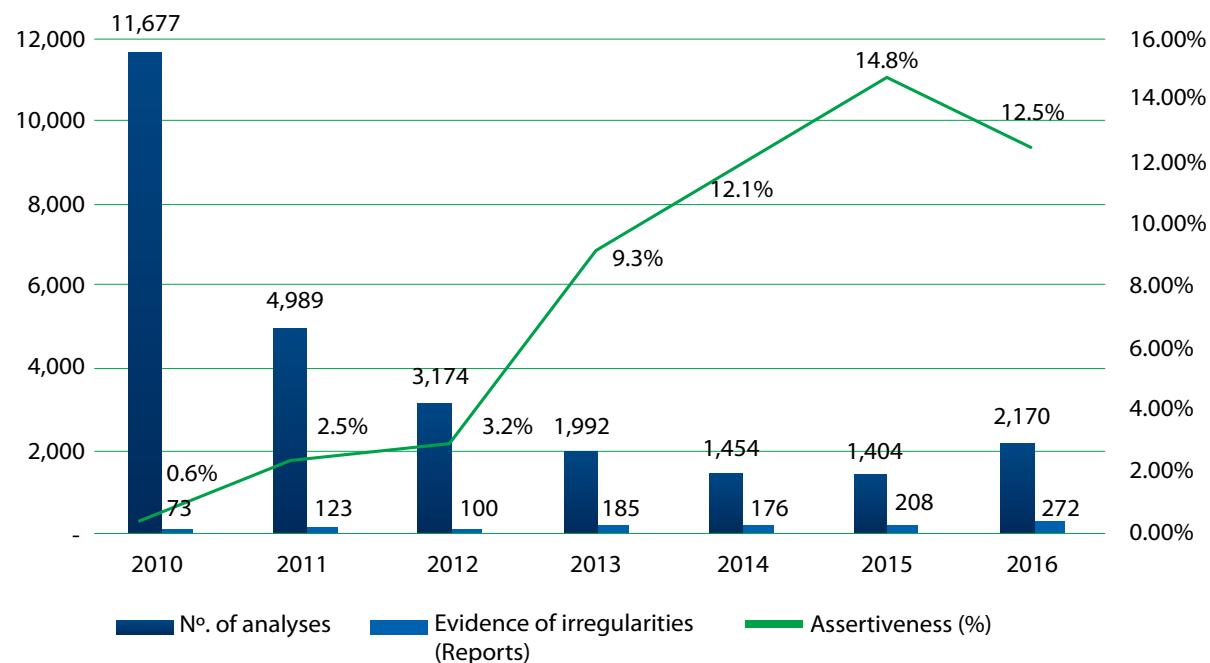


All bids, offers and transactions processed on BM&FBOVESPA's markets are analyzed by BSM's market surveillance systems. Alerts are issued when deviations that may relate to irregularities are detected, triggering investigation by BSM's specialists.

If necessary, BSM can ask the participants involved in suspicious transactions for clarification. If there is evidence of irregularities, a Market Oversight Report is opened to deal with the case.

In recent years BSM's technical staff has continuously enhanced the filters and parameters used by its supervision systems, leading to increased efficiency on the part of the technical team responsible for analyzing alerts. Chart 3 plots the rising assertiveness of BSM's analyses, resulting in more investigations triggered by alerts due to detection of trading irregularities.

Chart 3 – Assertiveness of market surveillance analyses



Market Oversight Reports

In 2016, BSM initiated 272 Market Oversight Reports and completed 242. Of these, 105 led to case dismissal, 63 led to the adoption of enforcement measures, and 74 were forwarded to CVM for treatment.

Cases forwarded to CVM typically relate to situations in which the offenders do not come within BSM's jurisdiction because they are not market participants accredited by BM&FBOVESPA (or their employees or agents).

DATA MINING SYSTEMS UPGRADE

In 2016, BSM's data mining tools were upgraded by the market supervision team, leading to a significant increase in the occurrences generated (63% growth year over year) and in the number of investigation reports initiated, which rose to 272, from 206 in 2015. The 2016 Market Oversight Reports also contained more precise information and more evidence to support the enforcement process.

Supervision of trading in securities issued by BM&FBOVESPA

BSM is responsible for analyzing transactions involving securities issued by BM&FBOVESPA, pursuant to CVM Instruction 461/2007, article 58, to ensure that the general rules for issuers are observed by BM&FBOVESPA as an issuer of shares for trading.

Summary of Market Supervision activities in 2016

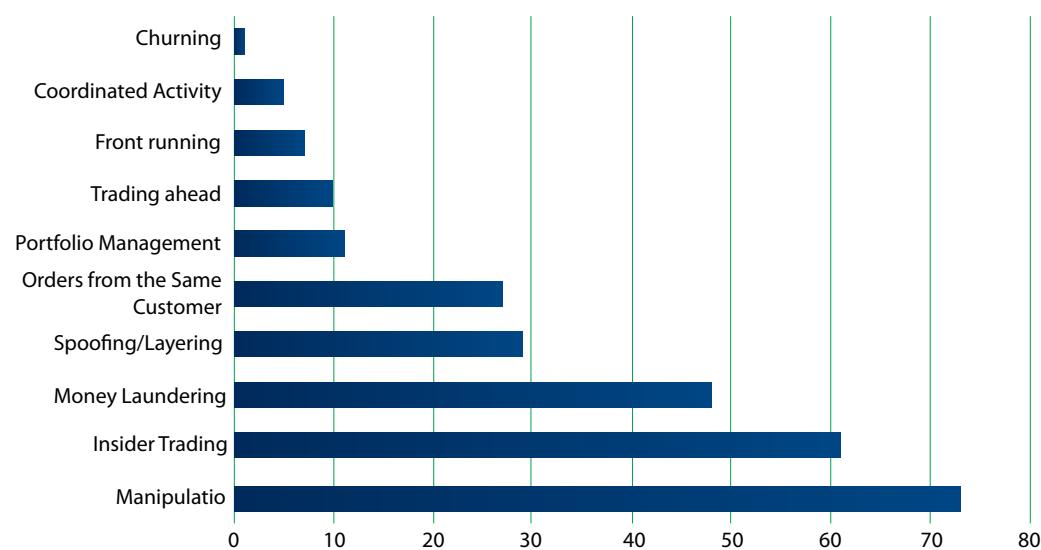
Table 5 summarizes BSM's market supervision activities in 2016.

Table 5: Market Supervision in Numbers

Reports initiated, completed and in progress	
Caseload (reports in progress) on January 1, 2016	85
(+) Reports initiated	272
(-) Dismissed	105
(-) Forwarded to CVM	74
(-) Enforcement measures	63
Caseload (reports in progress) on December 31, 2016	115

The 272 investigations initiated in 2016 can be grouped by irregular practice. Chart 4 shows the distribution of these abusive practices by frequency.

Chart 4. Infringements identified in Market Oversight Reports



In 2016, as can be seen from the figure, BSM's market supervision team analyzed cases involving suspected coordinated trading, irregular portfolio management, money laundering, order manipulation, self-trading, and insider trading, among other infringements.

LAYERING AND SPOOFING

In 2016, BSM investigated Latin America's first cases of alleged layering and spoofing in the capital markets. Layering and spoofing are forms of market manipulation that involve the creation of artificial conditions of supply and demand. They are considered illegal practices because they jeopardize market integrity and are banned under CVM Instruction 8/1979.

In the case of layering, a trader creates artificial buying or selling pressure and attracts others to trade by placing orders without intending to execute. These fake orders trick other market participants by producing a false impression of increased liquidity for the securities concerned and of heavy buying or selling pressure, depending on the interest of the trader who is using the layering strategy. This trader places an order on the opposite side of the book in order to match the order entered by the misled investor. The artificial orders are then canceled.

As defined by BSM, this abusive practice is characterized by a sequence of events that configure a trading cycle with the following stages:

- 1 Creation of false liquidity: the trader places several artificial orders on the opposite side to his position, forming layers of orders he has no intention of executing and changing the order book spread in order to attract orders from investors or trick them into improving their bids.
- 2 Investors' reaction to the registration of artificial orders and execution of a trade.
- 3 Cancellation: the artificial orders are canceled once the trade is executed.

In spoofing, a trader seeks to attract counterparties to match his order by placing large orders for the same securities on the opposite side of the market,

without any intention of executing them. The artificial pressure created by the large order leads market participants to raise their bids. When the price reaches the right level for the spoofer, he executes the order that interests him and cancels the large artificial order.

Thus the practice consists of creating artificial demand, supply or pricing in the presence of the following characteristic elements: closing of actual securities trades, intent to commit fraud, and alteration of the flow of buy or sell orders.

As defined by BSM, this abusive practice is characterized by a sequence of events that configure a trading cycle with the following stages:

- 1 Orders placed on both sides of the market.
- 2 A large order placed on the opposite side to the genuine order with the aim of creating buying or selling pressure and influencing other investors' trading decisions.
- 3 Investor reaction to the large order, and hence execution of a trade on the opposite side.
- 4 Cancellation of the large order.

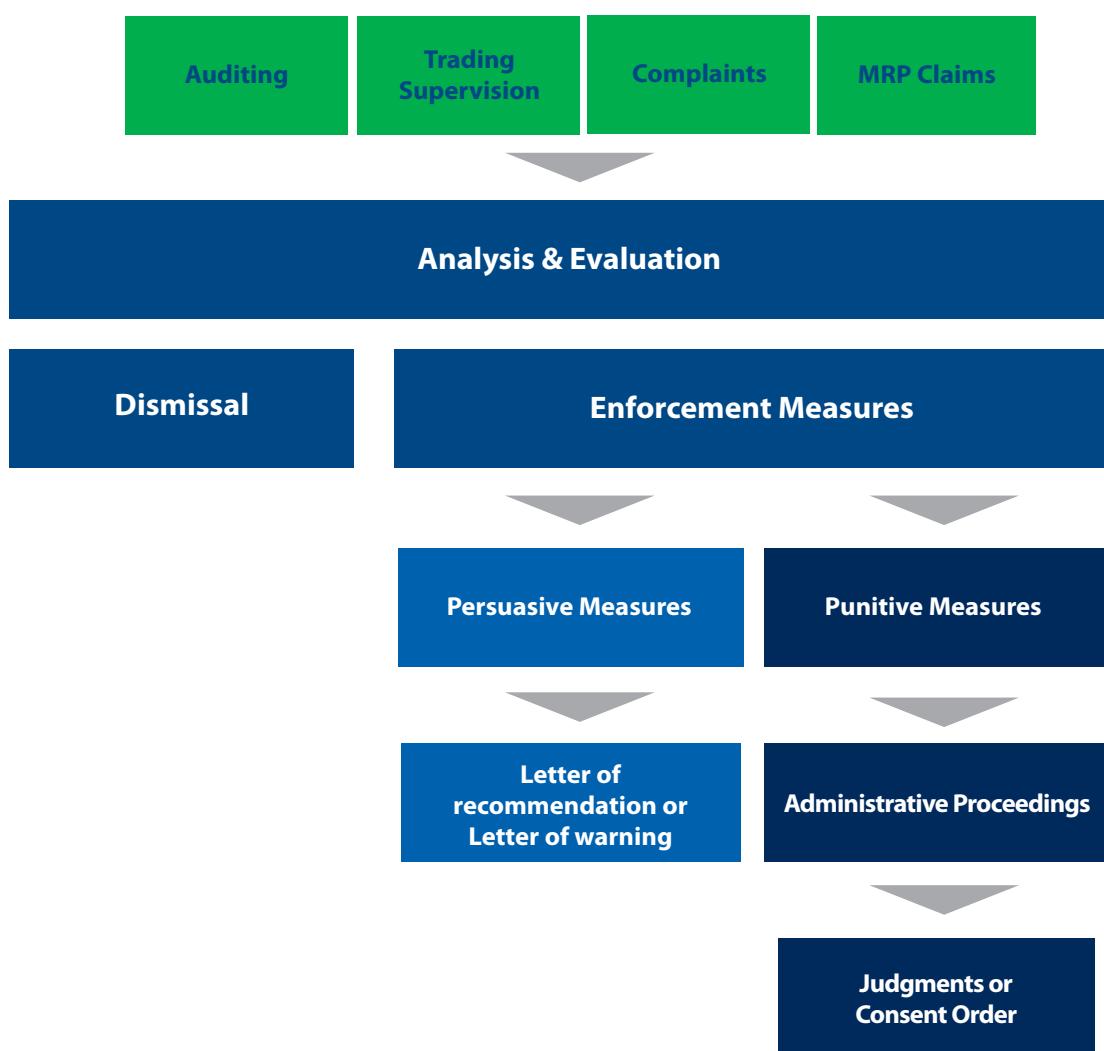
The cases investigated by BSM in 2016 involved criminal intent to alter the flow of trades by placing artificial orders and executing the one matched by an investor who placed the best order in response to the artificial demand or supply. The trade flow was altered because the artificial orders both signaled additional liquidity for the securities concerned and improperly altered the order book (or trade flow) with the intent of tricking other investors into placing new orders or modifying orders and executing at prices unfavorable to themselves but favorable to the trader who used the illicit layering or spoofing strategy.

Disciplinary Administrative Proceedings and Enforcement

An effective system of supervision requires adequate treatment of the problems and infringements identified by means of disciplinary measures, persuasion or the application of penalties, so that offenders can be given guidance or penalized and the problems remedied. These enforcement activities aim to improve the standard of participants' conduct, encourage the implementation of adequate internal controls by market institutions, penalize offenders, and prevent repetition of violations.

As shown in the next figure, analysis of the evidence of infringements detected by BSM's supervision activities, complaints received and MRP claims submitted may lead to enforcement actions, which range from recommendations that the institution improve its processes and controls to the initiation of disciplinary administrative proceedings (PADs), potentially resulting in the application of penalties by BSM.

Figure 3 – Simplified flow chart of enforcement activities



Letter of Recommendation and Letter of Admonition

When evidence of irregularities is detected but is not sufficient to justify administrative proceedings, the Chief Regulatory Officer may decide to send a Letter of Recommendation or a Letter of Warning as guidance and to prevent any future irregular activities.

Through a Letter of Recommendation the Chief Regulatory Officer recommends that the participant improve conduct, rules, procedures and/or in-

ternal controls, and may require that the participant implement an action plan to remedy the problems identified in the letter.

Letters of Warning are another enforcement instrument available to BSM, in which the Chief Regulatory Officer orders participants to cease an irregular practice and prevent its recurrence.

In 2016, BSM sent 128 Letters of Recommendation and 287 Letters of Warning. The Letters of Recommendation addressed the irregularities identified in indirect audits, including failure to comply with economic and financial requirements, and trading by persons linked to other participants.

Disciplinary Administrative Proceedings (PADs)

Infringements of laws, rules and regulations by participants in BM&FBOVESPA's markets may be judged in disciplinary administrative proceedings (PADs) held by BSM. These may involve not only BM&FBOVESPA's participants as institutions, but also their representatives (e.g. owners or directors) and agents (e.g. traders or self-employed investment agents).

PADs may result in the following penalties pursuant to BSM's bylaws:

- A warning
- A fine
- Suspension lasting up to 90 days
- Temporary disqualification lasting up to ten years
- Other penalties provided for in BM&FBOVESPA's rules and regulations

BSM's administrative proceedings observe constitutional procedural principles such as the right to a full defense and the right to an adversarial hearing, and are conducted in accordance with BSM's procedural rules, which have been approved by CVM.

PADs are judged in the first instance by the Chief Regulatory Officer (summary proceeding) or by a panel of BSM's Supervisory Board comprising three board members, at least two of whom must be independent (ordinary proceeding).

If convicted, the defendant may appeal to the plenary of the Supervisory Board.

A PAD may be halted by a consent order, which must be concluded before the first-instance judgment.

A consent order requires the defendant to cease the irregular practice that gave rise to the proceeding and pay compensation for any losses caused by

it. In addition, the defendant must undertake to prevent any repetition of the practice concerned, pay a monetary consideration to BSM, and implement controls relating to the facts of the case on the basis of an action plan with an execution timetable.

The PAD is closed if the consent order is carried out. If not, it continues to judgment.

In 2016, BSM analyzed 51 consent order proposals, approving five and denying four. In 42 cases, acceptance was conditional on an increase in the monetary penalty or implementation of one or more additional measures.

In 2016, BSM initiated 47 PADs involving 95 defendants. Table 6 shows a breakdown by type of defendant.

Table 6: Defendants in Disciplinary Administrative Proceedings Initiated in 2016

Type of Defendant	Nº.
Participants	21
Director of Participant	18
Traders	38
Self-employed Investment Agents	17
Managers of investment funds	0
Other	2
Total	96

BSM has substantially reduced the average time taken to finalize administrative proceedings, which was 125 days in 2016, compared with 208 days in 2015.

Tables 7 and 8 show a breakdown of the administrative proceedings by origin and the main problems that gave rise to them.

Table 7: Origin of Disciplinary Administrative Proceedings Initiated in 2016

Origin	Nº.
Market supervision	28
Participant audits	12
Investor Compensation Mechanism (MRP)	3
Letter	3
Complaints	1
Total	47

Forty-three of the PADs initiated arose from investigations conducted as part of BSM's supervision and inspection activities, while four arose from irregularities identified in proceedings relating to MRP claims⁵.

Table 8: Substance of Disciplinary Administrative Proceedings Initiated During 2016

Substance	Nº.	%
Artificial demand, supply or pricing of securities	20	39%
Irregular activities of Self-employed Investment Agents	6	12%
Conflicts of interest	4	8%
Non-compliance with working capital requirement	4	8%
Churning	3	6%
Fraudulent trades	3	6%
Non-compliance with BSM's orders	2	4%
Price manipulation	2	4%
Unfair practices	2	4%
Non-compliance with equity requirements	2	4%
Irregularities in custody transfer	1	2%
Money Laundering	1	2%
Inadequate use of cash and/or assets	1	2%
Total	51	100%

Table 9 shows the outcomes of the PADs completed in the period 2010-16, specifying the number of administrative proceedings completed, the number of defendants involved and, for all defendants in aggregate, the number of convictions, acquittals and consent orders. In the case of convictions, the penalties are also listed.

Table 9: Outcomes of Completed Administrative Proceedings

Year	PADs	Defendants ¹	Consent Orders	Judgments		Penalties				Total value ²
				Conviction	Acquittal	Warning	Fine	Suspension	Disqualification	
2010	7	9	7	2	–	–	1	–	1	1,028
2011	18	33	16	14	3	7	5	–	2	3,591
2012	7	15	7	6	2	4	1	1	–	900
2013	17	38	15	18	5	8	8	–	2	2,74
2014	45	86	51	24	143	12	12	–	–	6,659
2015	77	154	9	81	64	18	54	–	9	4,906
2016	70	149	38	76	35	14	55	1	6	6,186

¹ The sum of the monetary considerations paid pursuant to consent orders and convictions may exceed the number of defendants, since in some cases the defendant signs a consent order relating to some infringements and is convicted on other charges.

² Total value corresponds to the sum of the fines and monetary considerations pursuant to consent orders effectively paid to BSM in the year in question.

It is important to note that all decisions in administrative proceedings are public and available on BSM's website (in Portuguese)⁶.

⁵ Administrative proceedings may be initiated to judge irregularities identified during the investigation phase of MRP cases, regardless of the verdict reached in the latter (i.e. whether or not the investor's claim is accepted).

⁶ www.bsm-autorregulacao.com.br (menu Atividades disciplinares e processos/ Consulte os processos).



ADMINISTRATIVE PROCEEDINGS – 2016 HIGHLIGHTS

One of the highlights among the PADs completed in 2016 was PAD 12/2015, initiated in response to action by the participant and its director of market relations to block BSM's 2015 and 2016 operational audits, failure to provide information, infringing CVM Instruction 461/2007, article 52 (I & II), and later non-compliance with obligations established by BSM.

The judgment panel of BSM's Supervisory Board ruled that infringements had indeed taken place as charged, sentencing the participant to suspension for 90 days and the director to disqualification for one year. The plenary of the Supervisory Board upheld the decision on appeal.

Another highlight was PAD 02/2015, completed with the signing of a consent order in the total amount of R\$5 million, the highest monetary consideration paid to BSM as a condition for the conclusion of a consent order in its entire history.

The defendants were found guilty of buying and selling shares of OGXP3 stock in two trading sessions with the aim of manipulating the cash market for this stock and making a profit for a customer of the brokerage house on the customer's positions in Ibovespa futures contracts.

The OGXP3 price manipulation took place in the context of the rebalancing of the Bovespa Index (Ibovespa), since OGXP3 was to have a higher weight in the new theoretical portfolio for the index and fluctuations in its price would therefore have a more significant impact on the price of Ibovespa.

The defendants' intent was to drive down the price of OGXP3 during the trading session held on August 30, 2013, by selling and shorting the stock, and then driving the price up on September 2, 2013, so as to have the desired impact on the Ibovespa.



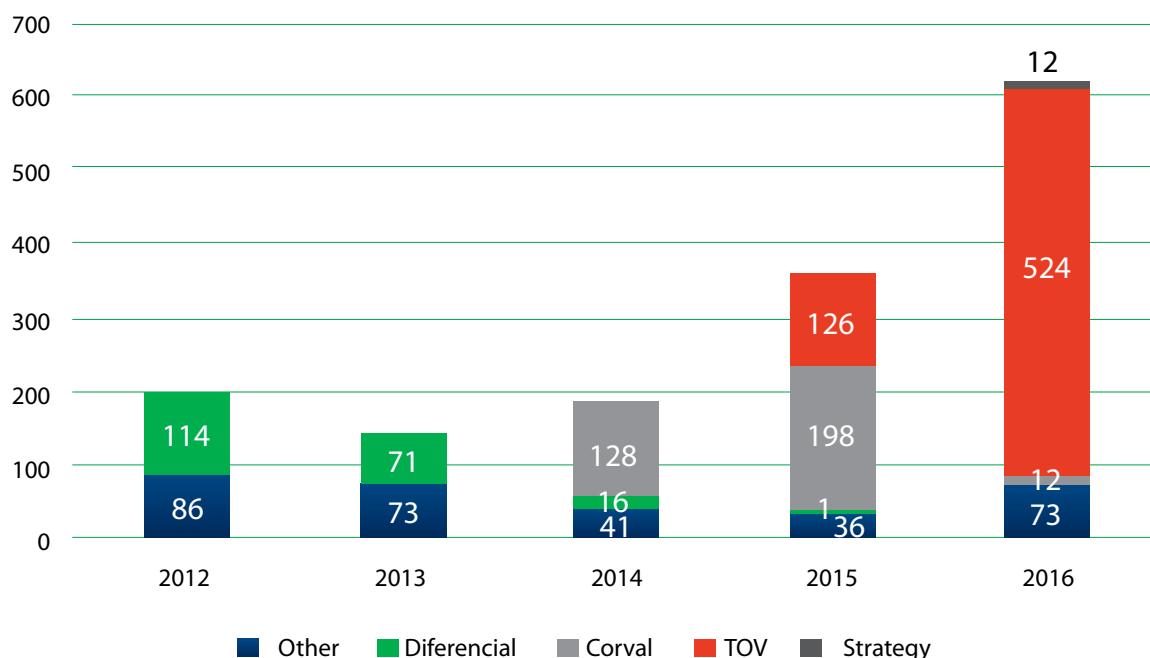
Investor Compensation Mechanism (MRP)

CVM Instruction 461/2007 requires all exchange markets to have an investor compensation mechanism to ensure that investors are compensated for losses resulting from action or omission attributable to market participants.

BSM manages BM&FBOVESPA's Investor Compensation Mechanism (MRP) and is therefore responsible for managing the fund and ruling on compensation claims filed by investors⁷.

Chart 5 shows the number of MRP claims in the past five years, highlighting the significant increase in the past three years due to out-of-court liquidation of Diferencial, Corval and TOV, brokerage houses that were participants accredited by BM&FBOVESPA⁸.

Chart 5 – MRP claims



In 2016, BSM successfully surmounted the challenge of analyzing, initiating and finalizing proceedings on the backlog of claims from customers of TOV in 120 days. Out of 524 claims filed by customers of this brokerage house, 404 were completed by December 31, 2016.

⁷ The status of claims files and BSM's ruling are available at www.bsm-autorregulacao.com.br (MRP / Processos MRP).

⁸ The Central Bank of Brazil ordered the out-of-court liquidation of Diferencial, Corval and TOV on August 9, 2012, September 11, 2014, and January 7, 2016, respectively.

MRP CLAIMS DUE TO LIQUIDATION OF TOV – VOLUME AND CASE COMPLETION STANDOUT

In 2016, BSM received 524 claims against the MRP to compensate investors for their current account balances with TOV CTVM Ltda., which were blocked owing to the out-of-court liquidation of the brokerage house on January 7, 2016.

The volume of claims filed in 2016 deriving from the blocking of current accounts with brokerage houses due to their out-of-court liquidation was substantial compared with previous years.

Despite this high volume, the fact-finding stage averaged 53 days and all cases were concluded in 120 days on average, complying with CVM Instruction 461/2007, article 78 (III).

Table 10 presents the number of claims received, completed and in progress since 2010. It is worth noting that in 2016 BSM again completed the processing of a record number of claims (504), and that the time taken to finalize cases averaged 146 days, down from 213 days in the previous year.

Table 11 shows the 504 claims completed in 2016 broken down by dismissals, denials and claims accepted. As can be seen from Table 12, the total amount of compensation paid in response to claims accepted in toto or in part was R\$7,215,676.22 in 2016⁹.

Table 10: MRP claims received, completed and in progress

	2010	2011	2012	2013	2014	2015	2016
Initial Caseload	173	160	119	167	185	183	85
Claims Received	122	54	200	144	185	235	620
Claims Completed	135	95	152	126	187	333	504
Final Caseload	160	119	167	185	183	85	201

Table 11: Claims completed in 2016

Decision	Nº.	%
Claims accepted	392	78%
Claims denied	80	16%
Claims dismissed	28	6%
Desistance of claimant	2	0%
Agreement between parties	2	0%
Total	504	100%

Table 12: Total Amount Compensated by the MRP (R\$ 000)

MRP Compensation	2011	2012	2013	2014	2015	2016	TOTAL
Brokerage houses liquidated out of court	–	–	293.30	542.20	4,367.90	6,841.90	12,045.30
Other Brokerage Houses	417.00	1,354.90	145.00	594.20	538.40	377.70	3,424.20
Total	417.00	1,354.90	438.30	1,136.40	4,906.30	6,974.80	15,469.50

⁹ Not including claims accepted in part where the plaintiff appealed to CVM and the appeal had not yet been heard.

\$ 17,351.50	▲ 24.7050	▲ 86.560	0.650	86.560	5.7540	5.7540	5.7540	+0.04
+90.45 0.43	▲ 47.0540	▲ 57.030	807.5	57.030	5.7540	5.7540	5.7540	+0.334
	▲ 6760.70	▲ 5.7540	0.607	5.7540	▲ 807.5	0.7540	0.7540	+0.10
	▲ 34.7080	▲ 0.7540	540.5	0.7540	▲ 540.5	86.560	86.560	+0.00
Global Stocks	EWPE	-WEF	EFF	-WEF	EFF	-WEF	-WEF	
\$ 15,551.50	▲ 16.0680	▲ 0.7040	405.4	2.2400	▲ 405.4	8.6350	8.6350	
+79.87 59	▲ 20.6500		054.0	4.9870	▲ 054.0	8.7860	8.7860	
				8.6350	767.6	5.3230	5.3230	
Technology Stocks			7.5030					
\$ 17,351.50	▲ 24.7050	▲ 86.560	0.650	86.560	▲ 0.650	57.030	57.030	
+90.45 0.43	▲ 47.0540	▲ 57.030	807.5	57.030		5.7540	5.7540	
	▲ 6760.70	▲ 5.7540	0.607	5.7540	▲ 807.5	0.7540	0.7540	
	▲ 34.7080	▲ 0.7540	540.5	0.7540	▲ 540.5	86.560	86.560	
Portfolio P1								
\$ 17,351.50	▲ 24.7050	▲ 86.560	0.650	86.560	▲ 0.650	57.030	57.030	
+90.45 0.43	▲ 47.0540	▲ 57.030	807.5	57.030		5.7540	5.7540	
	▲ 6760.70	▲ 5.7540	0.607	5.7540	▲ 807.5	0.7540	0.7540	
	▲ 34.7080	▲ 0.7540	540.5	0.7540	▲ 540.5	86.560	86.560	
Portfolio P2								
\$ 17,351.70	▲ 6760.70	▲ 5.7540	0.607	5.7540	▲ 807.5	0.7540	0.7540	
+87.45 0.00	▲ 34.7080	▲ 0.7540	540.5	0.7540	▲ 540.5	86.560	86.560	

	Price	Chg	%Chg	Shares
▲ 24.7050	▲ 86.560	0.650	86.560	▲ 0.650
47.0540	▲ 57.030	807.5	57.030	5.7540
▲ 6760.70	▲ 5.7540	0.607	5.7540	▲ 807.5
▲ 34.7080	▲ 0.7540	540.5	0.7540	▲ 540.5
				86.560
EWPE	-WEF	EFF	-WEF	EFF
▲ 16.0680	▲ 0.7040	405.4	2.2400	▲ 405.4
▲ 20.6500		054.0	4.9870	▲ 054.0
			8.6350	767.6
				5.3230

28.812	56,985	+56,985	+56,985	+56,985
247	478	+478	+478	+478
207	109	+109	+109	+109
500	770	+0.770	+0.770	+0.770
678	348	+0.2346	+0.2346	+0.2346

Notices to COAF

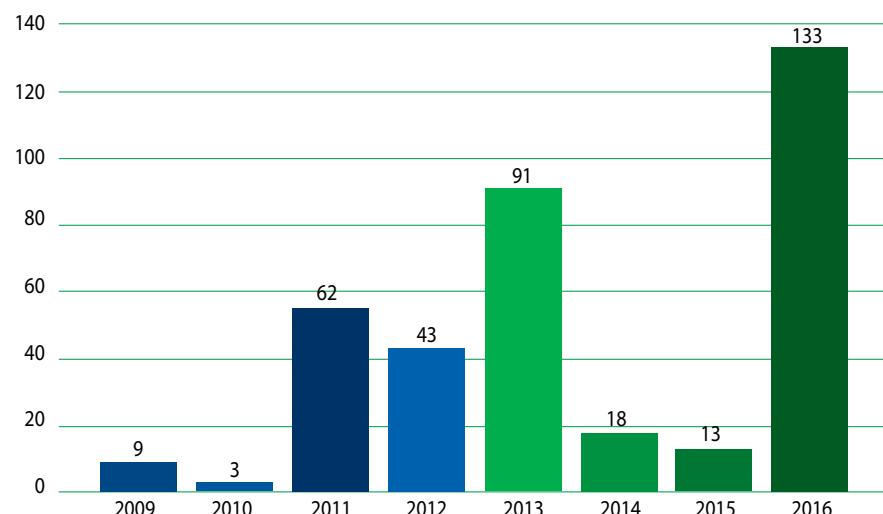
Law 9613/1998 and CVM Instruction 301/1999 require brokerage houses and other intermediaries, custodians, fund managers and other individuals or legal entities involved in certain activities to keep an up-to-date customer register and monitor customer transactions continuously, paying special attention to activities that may constitute evidence of money laundering.

Any suspicious activities must be reported to the Financial Activities Control Council (COAF), the government body responsible for preventing and combating money laundering and terrorism financing.

In the course of its supervision and inspection activities, BSM may come across situations that must be reported to COAF. In 2016, BSM filed 133 such notices with COAF.

BSM also works with BM&FBOVESPA's participants to emphasize the importance of maintaining controls designed to prevent the use of securities for money laundering, and to urge custodians and intermediaries to report suspicious activities to COAF.

Chart 6 – Notices filed with COAF by BSM



IMPROVEMENTS TO CVM INSTRUCTION 301/1999

In 2016, BSM worked with BM&FBOVESPA and CVM to enhance the rules and regulations that deal with the prevention of money laundering and terrorism financing in securities markets, proposing that CVM Instruction 301/1999 reflect best practices in the world's major markets including the latest recommendations of the Financial Action Task Force to Combat Money Laundering & Terrorist Financing (GAFI/FATF).

BSM's contributions sought to emphasize normative provisions that would require brokerage houses to define their criteria for classifying customer and trading risks, and establish evidence of inadequate implementation of anti money laundering (AML) rules, procedures and internal controls by brokerage houses, among other items.

With contributions from BSM and BM&FBOVESPA, on November 17, 2016, CVM published a notice convening a public hearing (SDM 09/2016) to obtain market contributions to the draft normative instruction on the prevention of money laundering and terrorism

financing ((PMLTF) in securities markets, replacing CVM Instruction 301/1999.

The main innovations in the draft are (a) the establishment of a risk-based approach to the prevention of money laundering and terrorist financing, (b) guidelines on the implementation of this approach in the segments regulated by CVM, requiring institutions to conduct internal risk assessments and introduce policies for the prevention of money laundering and terrorist financing, (c) designation of two senior officers to oversee compliance with obligations, (d) enhancements to know your customer (KYC) procedures including more flexible timeframes for updates to registration details, introduction of the concept of financial beneficial owner and definition of the KYC safeguards institutions are to put in place, (e) tighter requirements to notify the Financial Activities Control Council (COAF) regarding suspicious transactions, and (f) case-by-case analysis of abnormal activities detected by trade monitoring..



Institutional Relations

BSM is in constant touch with Brazilian securities markets regulators at CVM and the Central Bank, both to exchange information on surveillance, supervision and enforcement, and to discuss enhancements to legal norms and regulatory procedures.

BSM also interacts with other self-regulatory organizations and industry associations, such as: the Brazilian Association of Financial & Capital Market Institutions (ANBIMA), where BSM sits on committees for investment fund best practices, regulation and best practices for qualified capital market services, and regulation and best practices for financial instrument trading; and the National Association of Closed Pension Funds (ABRAPP), where BSM sits on the self-regulation committee.

BSM participates in the main international forums involving regulators and self-regulatory organizations, such as the International Organization of Securities Commissions (IOSCO).

It also participates in working groups and committees in these organizations, such as IOSCO's Affiliate Members Consultative Committee (AMCC). Affiliate members of IOSCO include other self-regulatory organizations and international associations.

BSM'S NEW WEBSITE

BSM launched a new website in July 2016 to improve communication with its various stakeholders. With a new architecture and the addition of new content, its sections were reorganized to facilitate navigation.

Among the main alterations were the inclusion of a search engine to query Investor Compensation Mechanism (MRP) claims and disciplinary administrative proceedings (PADs) using a number of filters.

The new website also enables users to search and read all the laws and regulations applicable to the securities markets, as well as presentations, materials for the workshops and other events organized by BSM, up-to-date statistics and information on its activities, and contact details for sending complaints and suggestions directly to the team responsible for dealing with them.

In 2016, BSM took part in IOSCO/AMCC's FinTech Working Group, which mapped the development of the main technologies used in capital markets and their regulatory impact. The results obtained by the working group served as input to IOSCO's Research Report on Financial Technologies (FinTech).

BSM seeks constant dialogue with all actors in the Brazilian markets, organizing events on relevant topics, including workshops to offer market participants guidance on specific issues.

The main topics addressed in 2016 were suitability, monitoring to prevent money laundering, and surveillance of orders to combat abusive market practices.



Education and Training

BSM's management prioritizes the highest possible qualifications for its technical staff and maintains an educational incentive program that awards scholarships to help pay for MBA and other master's courses and postgraduate studies. In 2016, nine employees received this benefit.

BSM also encourages staff to take specific training courses abroad, such as those offered annually by the Securities & Exchange Commission (SEC), which regulates the US stock market, and the Commodity Futures Trading Commission (CFTC), which regulates the US derivatives market.

BSM also brings experts from other countries to give courses to its staff and has held international seminars on relevant topics at its offices since 2011. The 2016 seminar focused on market supervision and enforcement in securities markets, featuring speakers from the SEC; the Financial Industry Regulatory Authority (FINRA), the main self-regulatory organization for the US securities industry; the Bombay Stock Exchange; the University of Chile; CVM; and BSM itself.

Table 13: Events organized by BSM

Event	Date
International training seminar on market supervision and enforcement in securities markets	November 7-8, 2016
Workshop on monitoring abusive securities market practices, money laundering prevention and internal controls	November 23, 2016

Some 100 people took part in this training seminar, including guests from CVM, the Central Bank, ANBIMA, ANCORD and CETIP, as well as the staff of BSM and BM&FBOVESPA.

Representatives of BSM also participate as speakers in BM&FBOVESPA's Educational Institute, in the TOP for Teachers program to disseminate knowledge about capital markets, and the Regulators Program for representatives of public and private regulatory and self-regulatory organizations.

To this end BSM has a four-person administrative team whose main activities are described in the next chapter.

A close-up photograph showing a person's hands holding a blue smartphone horizontally. The phone is positioned above a white laptop keyboard. The background is slightly blurred, suggesting an office environment.

Administrative Activities

BSM's secretariat and administrative support unit plays a vital role in enabling the organization to carry out its activities with maximum efficiency.

Its main tasks are as follows:

- Drafting, sending, receiving and controlling correspondence
- Scheduling and controlling internal and external meetings, travel and other engagements
- Drafting, checking and sending applications for reimbursements and payments (Supervisory Board, CRO, managers, staff)
- Booking flights and accommodation (Supervisory Board, CRO, managers, staff)
- Controlling office material, equipment, conference rooms, subscriptions to periodicals
- Documentation – assembling case files, digitizing and filing
- Personal and telephone service

Table 14 summarizes the key statistics for these activities.

Table 14: Main secretariat and administrative support activities

Activity	Total 2016	Monthly average
Correspondence items sent	6,552	546
Correspondence items received	3,407	284
Document digitizing – pages scanned	160,876	13,406
Meetings with participants	300	25
Processing of receipts (travel expenses, taxis etc.)	1,014	85
Flight and hotel bookings	1,206	101

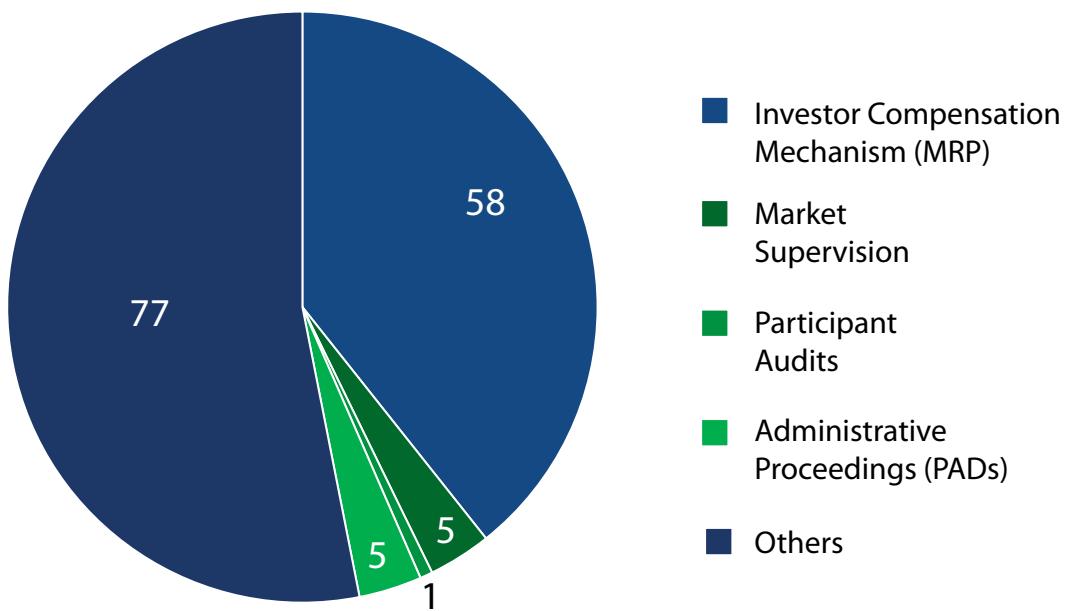


Public Information Service (SAP)

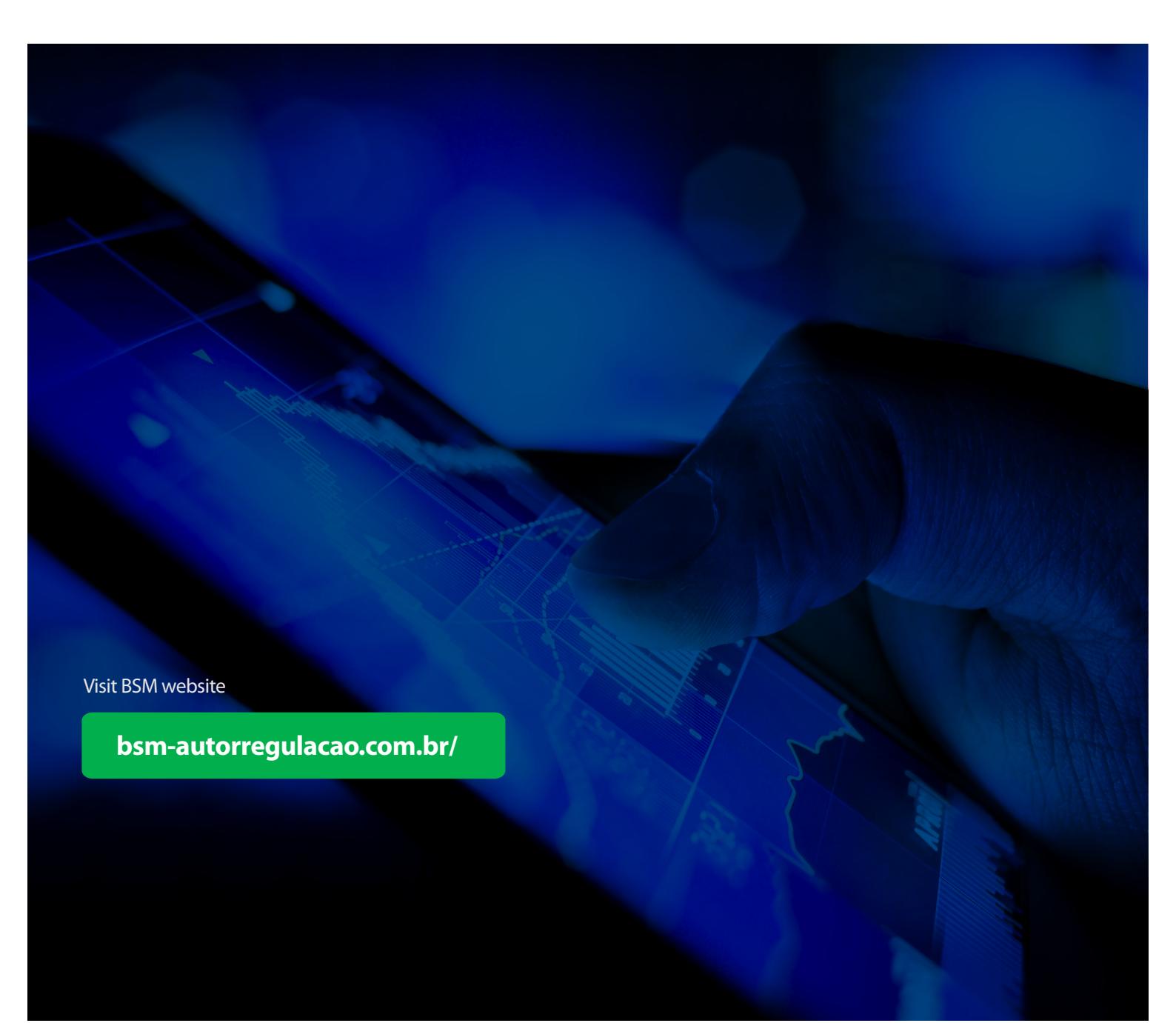
BM&FBOVESPA and BSM maintain a Public Information Service (local acronym SAP) to receive requests for information, criticisms, and suggestions on the activities of BM&FBOVESPA and its participants as well as BSM itself. It can be accessed by phone, online, and in person at BSM's offices.

In 2016, BSAM received 146 comments, complaints or requests for information on the topics shown in Chart 7.

Chart 7 – Public Information Service (SAP) – Main types of information request, comment or complaint



Most of these contacts consisted of queries from investors who wanted to know the status of their MRP claims. It is important to note that up-to-date information on the status of MRP claims is available from BSM's website.



Visit BSM website

bsm-autorregulacao.com.br/



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