



# Activities Report

2017

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**BSM**  
MARKET SUPERVISION



# Mission

We protect the integrity of the markets managed by B3 and the investors who trade on them.

# Mandates

- Supervise market activities (orders and trades) to identify any abnormality or behaviors capable of putting at risk the regular functioning and credibility of B3's markets;
- Inspect B3's Participants' compliance with the applicable laws, regulations and rules;
- Oversee B3's activities as an issuer of listed securities and administrator of securities markets;
- Conduct disciplinary administrative proceedings to investigate irregularities, and penalizing offenders;
- Manage the Investor Compensation Mechanism;



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# Introduction

The evolution of the securities market obliges regulators and Self-Regulatory Organizations to continuously update and refine their work methods and supervision techniques. At the same time they must increasingly interact with market participants to ensure that trading is conducted with integrity and transparency on a market that properly fulfills its intermediation and price formation functions.



In March 2017, BM&FBOVESPA and CETIP merged leading to the creation of B3 – Brasil, Bolsa, Balcão ('B3'), the fifth largest exchange in the world by market value.

In 2017, BSM made changes to its corporate bylaws and Procedural Regulation to provide for BSM's self-regulating activities in regard to the CETIP segment.

Over the course of 2017, BSM's self-regulating work plans for the BM&FBOVESPA and CETIP segments were concluded separately.

As of 2018, BSM's self-regulating activities in both segments will be carried out jointly in accordance with the budget and work plan to generate efficiency and reduced costs for Participants.

Seeking to assure the correct functioning of the markets managed by B3, in 2017 BSM introduced important enhancements to its auditing, market surveillance and enforcement activities and promoted initiatives to increase communication and transparency with regulators and the general public.

One of the main attributions of BSM is to guide and encourage the creation of a culture of compliance and the enhancement of internal controls at the market participants' organizations.

We have thus continued to provide seminars that offer Participants guidance and clarification. In a seminar held in the second half of 2017, we covered issues regarding the role of data mining and technological tools to combat money laundering in the financial and capital markets.

Within the scope of our audit activities we have extended the coverage of operational audits held with Participants in the markets managed by B3 by including operational audits in the work plan with custodians, settlement agents, gold depositories and securities registrars, bearing in mind the regulatory changes made by the Brazilian Securities and Exchange Commission (CVM).

BSM also prioritized enhanced communications and greater transparency in 2017. For this reason, the BSM website was remodeled to contain new content and functionality in the Investor Compensation Mechanism, which will join a totally digital platform at the start of 2018.

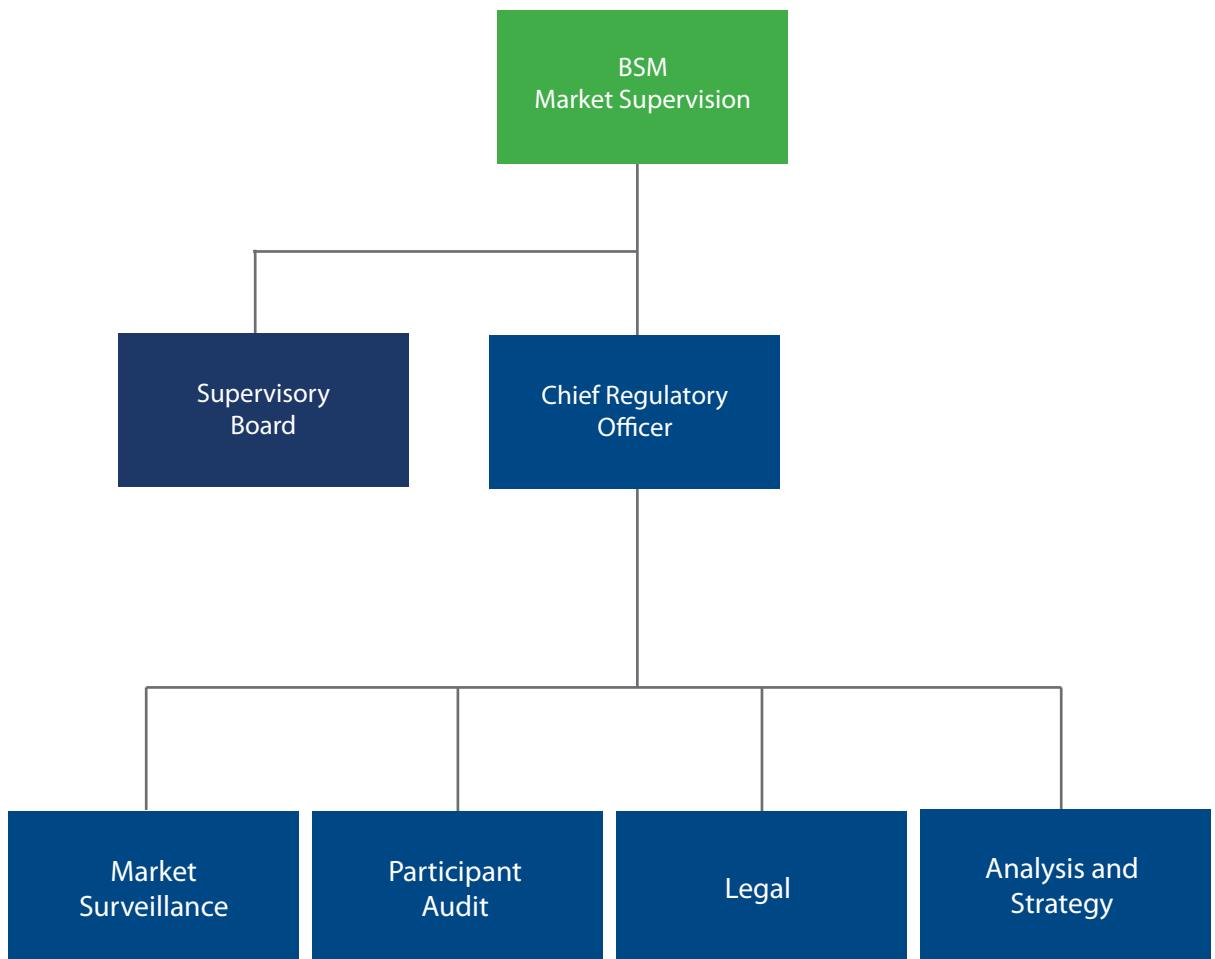
Finally, we wish to emphasize BSM's efforts towards the constant enhancement of activities, which has resulted in improvement to its Supervision Risk Classification by CVM, as reported in that body's Biennial Risk-Based Supervision Plan<sup>1</sup>.

<sup>1</sup> CVM's biennial plans are available at: [http://www.cvm.gov.br/menu/acesso\\_informacao/planos/sbr/sbr.html](http://www.cvm.gov.br/menu/acesso_informacao/planos/sbr/sbr.html)

As reported in the Biennial Risk-Based Supervision Plan, CVM considered there to be less of a likelihood in the 2017-2018 biennium of the occurrence of failures in the inspection of trades executed in the exchange and OTC markets (risk event nº 1); of inspection failures by intermediaries and their agents (including self-employed investment agents), custodians and registrars (risk event nº 2); and of failures in the instruction and conclusion of sanctioning administrative proceedings (risk event nº 3), maintaining as low probability the occurrence of failures in handling complaints to the Investor Compensation Mechanism.

In the following pages we present details of the activities performed by BSM and the main highlights of our activity in 2017.

Figure 1  
BSM Organizational Chart



Note: The Supervisory Board has 11 members with voting rights, as well as the Self-Regulation Officer, who does not have voting rights as set forth in the BSM Bylaws.



# Participant Audit

BSM is responsible for the inspection and direct audit of Participants in the markets managed by B3, which occurs through audits of Participants to assess compliance of their processes and controls with legal and regulatory rules.

## Pre-Operational Audit

In order to be authorized as a Participant in the markets managed by B3, an institution must meet a series of operational, technical and financial requirements that comprise the rules for authorization and maintenance of access to B3.

BSM checks compliance with these requirements in the pre-operational audit held at the institution that requests access to B3. As illustrated in Table 1, BSM held 11 pre-operational audits in 2017.

## Operational Audit – Trading Participant

Operational audits of Full Trading Participants and Trading Participants assess processes, controls and technological infrastructure, such as information security; business continuity; suitability; customer registration; order reception, registration and execution; trade settlement; custody of assets; risk; and administration of investment clubs and self-employed investment agents linked to the Participant.

Within the scope of operational audits, BSM also holds inspections of the self-employed investment agents that are linked to the Participants. In these inspections, BSM checks, among other things, the physical and technological structure of these agents, as well as their activities. In 2017, BSM inspected 719 self-employed investment agents linked to Full Trading Participants and Trading Participants.

## Operational Audit – Registration Participant

Operational audits of Registration Participants assess the controls applied for compliance with the minimum requirements for asset registration and custody processes, such as the registration and update of the asset's characteristics with B3 and checking the guarantee of the assets registered at B3, with the purpose of assessing whether asset registrations executed by Registration Participants at B3 and their respective supporting documents are complete, valid and up-to-date.

## Operational Audit - Custodian

Operational audits of Custodians assess the controls applied for compliance with the minimum requirements of custody processes for assets and positions, such as the opening and maintenance of investors' registrations; formalization and content of agreements for provision of custody services; control of the amounts in balance, of transfers and of corporate actions in-

volving the assets under custody; daily matching of asset positions; providing investors with information that allows the identification of events involving securities; information security; and IT infrastructure.

## Operational Audit - Registrar

Operational audits of Registrars assess the controls applied for compliance with the minimum requirements for asset registration processes, such as opening and maintaining the ledger book; registration of information about titles, rights, encumbrances and corporate actions regarding securities; daily matching of positions registered in the Registrar's controls and the registrations held and entered by the B3 Central Securities Depository; contents of the registrar service provision agreements; safekeeping and maintenance of documents related to book-entry securities registered at B3; surveillance; and IT infrastructure.

## Operational Audit – Gold Depository

Operational audits of Gold Depositaries assess the controls applied for compliance with the minimum requirements of gold custody processes, such as deposit, withdrawal and transfer of gold bars; checking and validation of gold delivered to and withdrawn from the Gold Depository; and IT technology.

## Indirect Audit

Indirect audits combine information obtained from a range of sources and treated with statistical software. In this way as a complement to direct audits, BSM assesses Participants' compliance with applicable rules and regulations by analyzing the entire universe of information instead of just samples.

The following items were indirectly audited in 2017

- Participants' compliance with the economic and financial requirements established by B3's rules
- Related-party transactions and own-account transactions by the Participant
- Analysis of current accounts of Participants' investors and partners to detect irregular extension of credit to customers
- Investor portfolio turnover and churning<sup>2</sup>

<sup>2</sup> Churning is excessive trading by a broker in a customer's account, largely to generate commissions

- Verification of compliance by Participants with their own Operational Rules and Parameters
- Certification of professionals

## DMA Audit

Direct Market Access (DMA) occurs when an investor accesses B3's trading system directly by means of an automated connection. Four categories of DMA are currently available for direct access to B3<sup>3</sup>.

Regardless of the DMA model used, an investor can only access B3's trading environment through a B3 Participant, who is responsible for monitoring customers' trades and setting their trading limits.

To preserve market integrity, it is important for Participants to have adequate pre-trading risk control systems, i.e., systems that check whether orders entered and positions held by customers comply with certain prerequisites.

BSM is responsible for auditing these pre-trading risk control tools when requested to do so by B3. In 2017 one tool was audited.

## MRP Audit

MRP audits are performed to clarify technical issues in proceedings relating to claims against the Investor Compensation Mechanism (MRP)<sup>4</sup>. In 2017, BSM produced 172 audit reports for MRP proceedings

## 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 B3's CEO. In 2017, BSM performed 21 special audits.

BSM offers a channel on its website for complaints by the general public. All complaints received are assessed and BSM takes necessary action to address them.

<sup>3</sup> Details of B3's Direct Market Access (DMA) models can be obtained from B3's website (Services / Trading Solutions / Direct Market Access (DMA)).

<sup>4</sup> For more information about the MRP, see the relevant section in this Report.

## Audits performed in 2017

Table 1 presents the number of audits performed by BSM in 2017 and Table 2 the interaction with the market by the auditing team.

Table 1  
Audits Performed in 2017

Type of Audit	Quantidade
Operational – Trading Participants (Brokers and Dealers)	64
Operational – Registration Participants	7
Operational - Custodians	2
Operational – Settlement Participant	1
Operational – Registrar Participant	1
Operational – Self-Employed Investment Agents	719
Indirect Audit	N/A
Pre-Operational	11
Special Audits	21
DMA Audit	1
Investor Compensation Mechanism (MRP)	172
<b>Total</b>	<b>999</b>

Table 2  
Interactions with the Market in 2017

Activity	
Consultations Answered for Market Participants	618
Meeting with Market Participants	221
Meeting with B3	44
Consultations answered for B3	31
<b>Total</b>	<b>914</b>

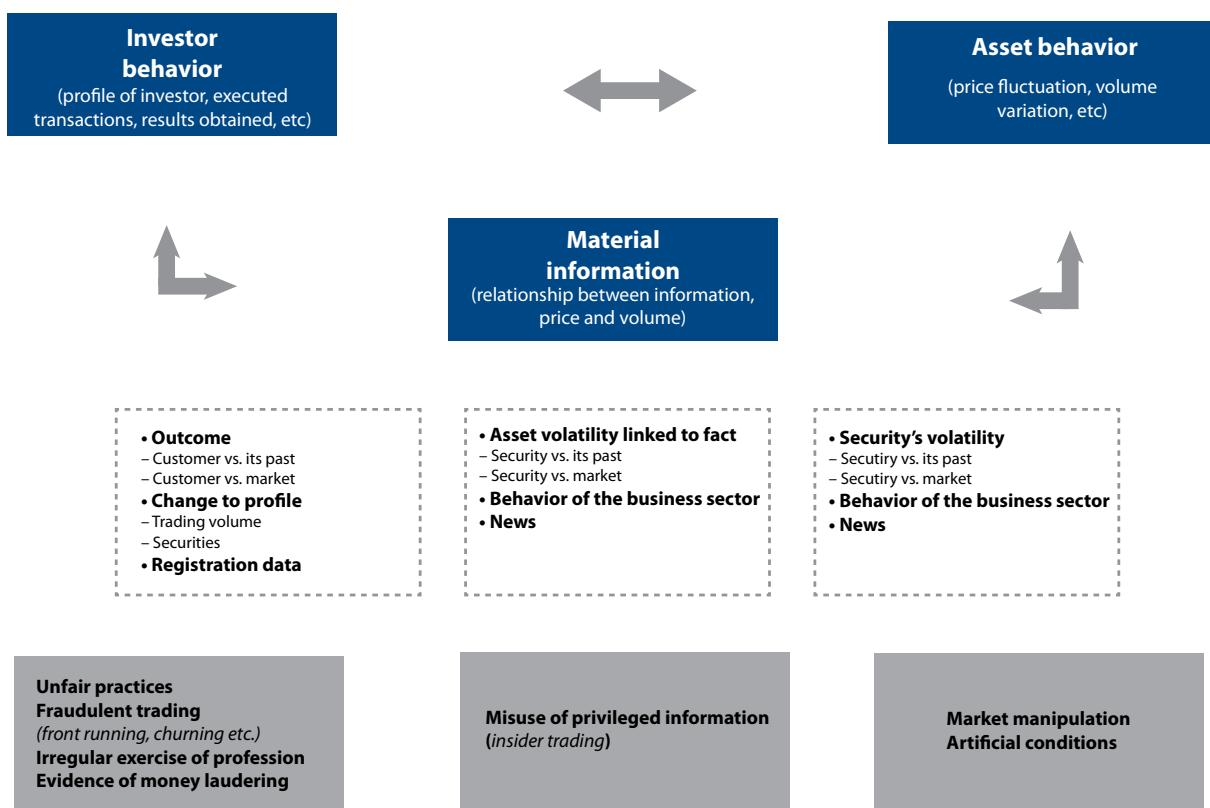


# Market Surveillance

BSM's market surveillance activities consist of monitoring the market 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. Figure 2 below shows BSM's market surveillance procedures in summarized form.

Figure 2  
Dimensions of Market surveillance



All bids, offers and transactions processed on B3'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 address the issue.

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.

## SHARING OF INDICATORS

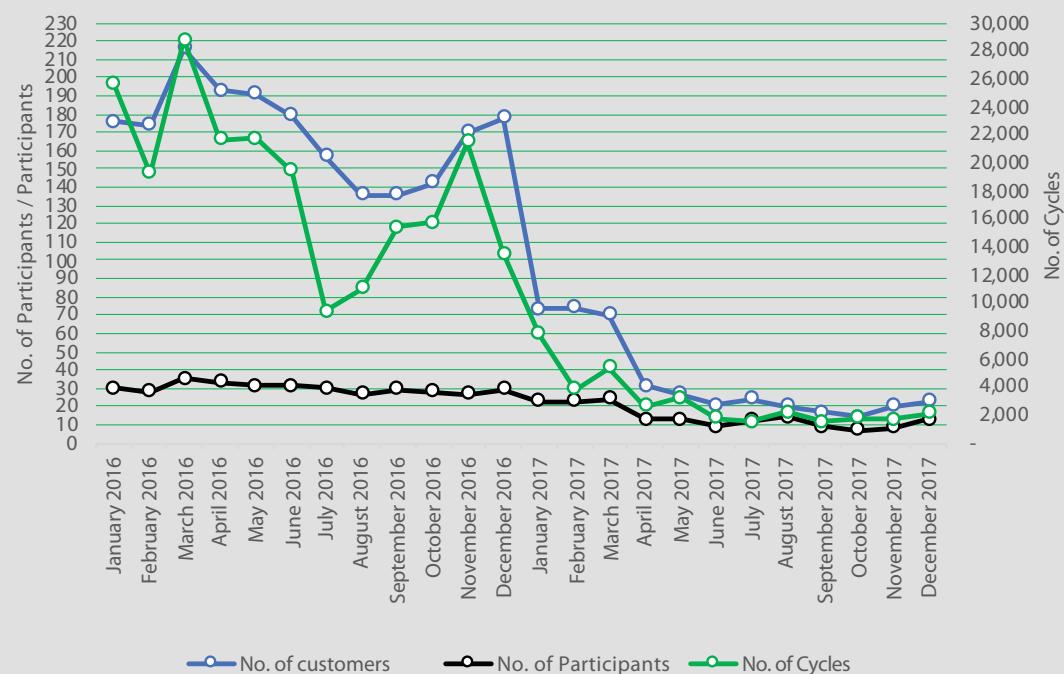
In April 2017, BSM shared with B3's Participants alerts about layering and spoofing practices.

The twice-monthly alerts identify activities that raise layering and spoofing suspicions, which Participants should analyze and, if they conclude there have been irregularities, act to prevent repetition thereof. The Participant must submit a response to BSM stating: (i) the conclusion of analyses and (ii) the measures adopted to prevent the abusive practice, when there has been such.

BSM devised a tool and submitted it together with the alerts in Excel. It reproduces the order book and allows cases flagged up in the alerts to be analyzed. The use of the tool is not mandatory and it seeks to aid Participants' analysis. BSM also held a workshop to disclose the procedure and gave training sessions for the Participants, which can be seen at <<http://www.bsm-autorregulacao.com.br/publicacoes-e-eventos/treinamentos-e-workshops>>.

The **Chart 1** below evidences the reduced number of spoofing and layering alerts. Several measures contributed to fewer occurrences of these practices, such as workshops and meetings to clarify the irregular nature of these practices, and enforcement actions against Participants that did not prevent layering and spoofing practices from continuing. To date, BSM has commenced nine Administrative Proceedings against 17 offenders.

Chart 1



## SHARING OF MONEY LAUNDERING ALERTS

Since November 2017, BSM has shared with Participants alerts that are generated pursuant to subparagraphs II and VII of article 6 of CVM Instruction 301. The purpose is to aid the market in surveillance of money laundering events so that the Participants can act in a timely manner in such cases.

The alerts are sent twice a month and identify apparent cases of money laundering. Participants have a duty to carry out analysis and, where there is evidence of the transfer of money among customers, report it to COAF. Participants must submit the conclusion of their analysis to BSM as well as the measures adopted and the communication to COAF when there is such.

In addition to this, BSM has held Money Laundering Prevention workshops and training sessions so that the market is better able to identify these operations and contribute to market integrity. The training material is available at the following link <<http://www.bsm-autorregulacao.com.br/publicacoes-e-eventos/treinamentos-e-workshops>>.

general rules for issuers when it performs the role of issuer of listed equities.

## Summary of Market Surveillance activities in 2017

**Table 3 and Chart 2** summarize BSM's Market Surveillance activities in 2017.

Table 3  
Reports Initiated, Completed and in Progress

Reports' Status	Qtde.
<b>Caseload (Reports in progress on Jan. 01, 2017)</b>	<b>115</b>
(+) Initiated	204
(-) Dismissed	128
(-) Forwarded to CVM	104
(-) Forwarded for enforcement	34
<b>Caseload (Reports in progress on Dec. 31, 2017)</b>	<b>53</b>

## Market Oversight Reports

In 2017, BSM initiated 204 and completed 266 Market Oversight Reports. Of these, 128 led to case dismissal, 104 led to the adoption of enforcement measures, and 34 were forwarded to CVM for treatment.

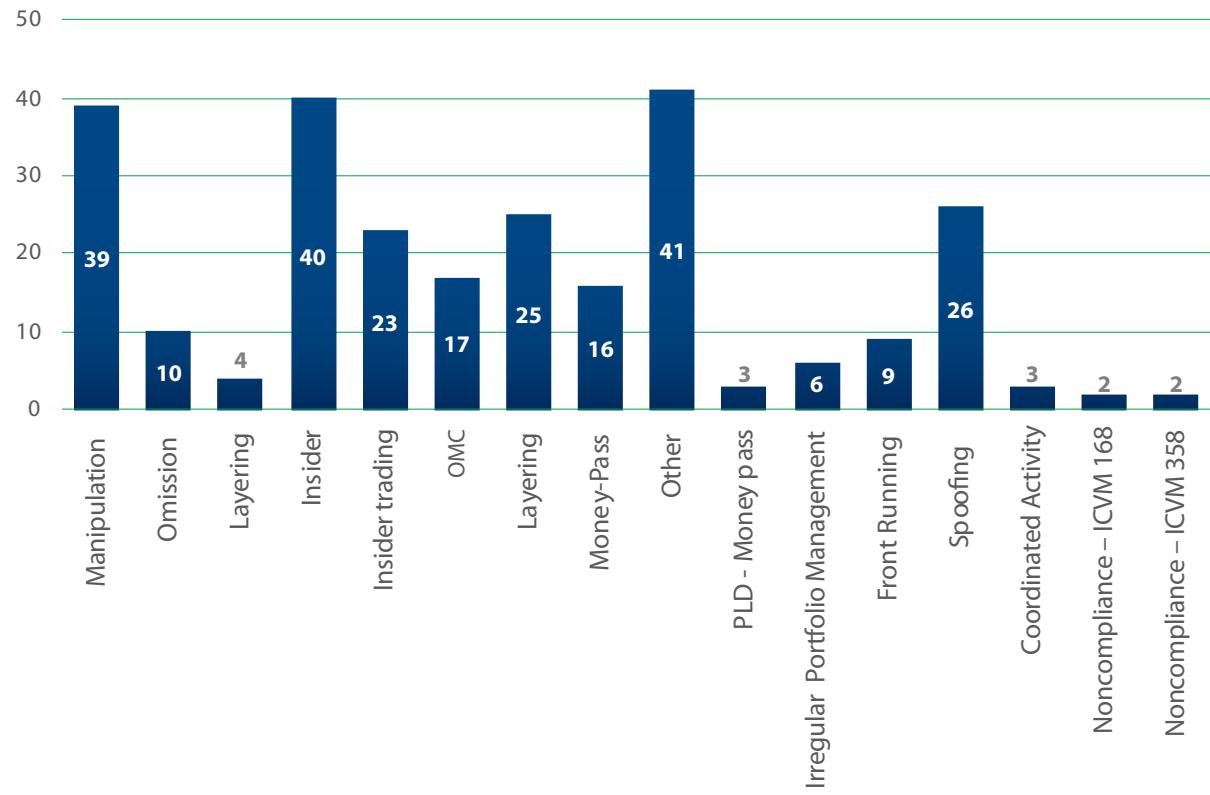
Cases forwarded to CVM typically relate to situations in which the offenders do not come within BSM's remit because they are not Participants of B3 (or their employees or agents).

## Supervision of securities issued by B3

BSM is responsible for analyzing transactions involving securities issued by B3, pursuant to CVM Instruction 461/2007, article 58, to ensure that B3 complies with the general rules for issuers when it performs the role of issuer of listed equities.

**Graph 2** shows the distribution of the 266 finalized reports based on the frequency by abusive practice.

Gráfico 2



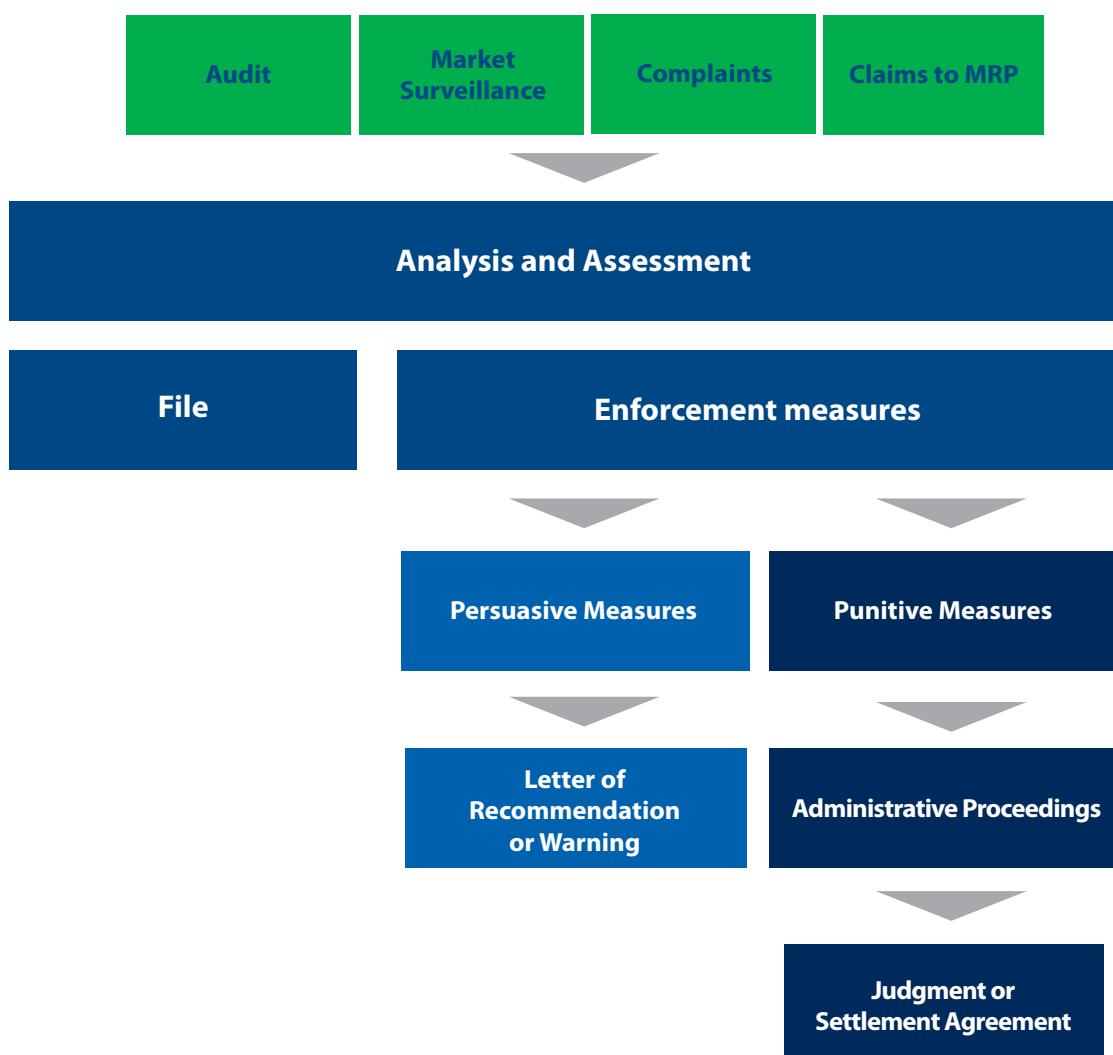
As can be seen from the chart above, in 2017 BSM's Market Surveillance team analyzed a few cases involving suspected coordinated trading, irregular portfolio management, money laundering, order manipulation, self-trading, and insider trading, among other infringements.

# Enforcement

An effective supervision system requires adequate treatment of the identified problems and infringements, by means of education, 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 **Figure 3**, analysis of evidence of violations 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 commencement of disciplinary administrative proceedings (PADs), potentially resulting in the application of penalties by BSM against Participants in the markets managed by B3 and by their agents.

Figure 3  
Simplified flowchart of enforcement activities



## Letter of Recommendation and Letter of Warning

Within the scope of BSM's supervision activities, when evidence is detected of irregularities insufficient to justify disciplinary administrative proceedings, but which require the Participant's attention, BSM may decide to send a Letter of Recommendation or a Letter of Warning as guidance and to prevent any future irregular activities.

In the Letter of Recommendation, BSM recommends that the Participant improve conduct, rules, procedures and/or internal controls, and may require that the Participant implement an action plan to remedy the problems identified in the letter. In this Action Plan, the Participant must single out the measures that will be adopted and the respective implementation timeframe.

Letters of Warning are another enforcement instrument available to BSM, in which Participants are ordered to cease an irregular practice and prevent its recurrence.

Submission of the Letter of Recommendation or Letter of Warning is not a prerequisite for opening Disciplinary Administrative Proceedings and the history of these letters' submissions to Participants can be considered aggravating circumstances favoring a penalty imposed by Disciplinary Administrative Proceedings, if there is a recurrence.

In 2017, BSM sent 149 Letters of Recommendation, 218 Letters of Determination and one Letter 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 B3's markets may be judged in disciplinary administrative proceedings (PADs) held by BSM. These may involve not only B3's Participants as institutions, but also their agents (e.g. partners or directors) and agents (e.g. traders or self-employed investment agents).

PADs may result in the following penalties pursuant to BSM's Bylaws regarding B3's BM&F and BOVESPA segments:

- A warning;
- A fine;
- Suspension lasting up to 90 days;

- Temporary disqualification lasting up to 10 years;
- Other penalties provided for in B3'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 and which are available on its website<sup>5</sup>.

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 offender may appeal to the plenary of the Supervisory Board, which is made up of its 11 members.

Within the scope of the Administrative Proceedings, the Settlement Agreement can be signed at any time as long as the offender presents the proposal by the date on which the case is judged at the first instance. The BSM Supervisory Board analyzes the Settlement Agreement proposal and it may accept it, reject it, or make it conditional, bearing in mind the opportunity and convenience of signing the Settlement Agreement, as well as the nature and seriousness of the infractions that have been analyzed, the prior record of the offenders, procedural economy, and the realistic possibility of punishment in concrete cases.

The Settlement Agreement requires the offender to cease the irregular practice that gave rise to the proceeding and pay compensation for any losses caused by it.

The Settlement Agreement carries no weight in regard to the confession of facts, nor to recognition of the illicit nature of conduct analyzed by the PAD.

If there is compliance with the Settlement Agreement, the PAD will draw to a close. If there is noncompliance with the Settlement Agreement the PAD will remain on its regular course and proceed to judgment.

In 2017, BSM analyzed 61 Settlement Agreement proposals, of which ten were approved and two were rejected. In 49 cases, acceptance was conditional on an increase to the monetary penalty or on implementation of one or more additional measures.

In 2017, BSM commenced 25 PADs. In addition to this were three proceedings where the Participants and their respective agents involved in the apparent irregularities investigated by BSM presented Settlement Agreement proposals prior to the commencement of the PAD. These 28 enforcement measures involved 50 offenders. **Table 4** shows a breakdown by type of

<sup>5</sup> <http://www.bsm-autorregulacao.com.br/assets/file/leis-normas-regras/Regulamento-Processual-da-BSM-18122017.pdf>

offender.

Table 4  
Offenders in Disciplinary Administrative Proceedings Commenced in 2017

Type of Accusation	Nº.
Self-Employed Investment Agent	14
Director of Participant	12
Trader	11
Participant	13
<b>Total</b>	<b>50</b>

In 2017, BSM finalized all of the old administrative proceedings that were still in progress. On December 31, 2017, the oldest proceeding was PAD-006/2016.

For proceedings commenced in 2016 and finalized in 2017, the average term until conclusion was 199 days from commencement until the final decision.

**Table 5** shows the origin of administrative proceedings.

Table 5  
Origin of the Disciplinary Administrative Proceedings Initiated in 2017

Origin	No.
Market Surveillance	14
Investor Compensation Mechanism	5
Complaints	1
Participant Audits	8
<b>Total</b>	<b>28</b>

Of the PADs initiated, 14 arose from investigations conducted as part of BSM's supervision and inspection activities, while five arose from irregularities identified in proceedings relating to MRP claims<sup>6</sup>, eight were identified through operational and special audits and one proceeding arose from an accusation submitted to BSM.

**Table 6** shows the outcomes of the PADs completed in the period 2010-2017, specifying the number of administrative proceedings completed, the number of offenders involved and, for all offenders in aggregate, the number of convictions, acquittals and Settlement Agreements. In the case of convictions, the penalties are also listed.

<sup>6</sup> 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).

**Table 6**  
Results of Completed Administrative Proceedings

Year	Nº PADs	Nº Offender <sup>1</sup>	Settlement Agreement	Judgments			Penalties			Total Value <sup>2</sup> (R\$ thousand)
				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	2,740
2014	45	86	51	24	14 <sup>3</sup>	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
2017	32	69	58	9	2	2	5	2	-	13,104

- (1) The sum of the monetary considerations paid pursuant to Settlement Agreements and convictions may exceed the number of offenders, since in some cases the offender signs a Settlement Agreement 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 Settlement Agreements effectively paid to BSM in the year in question.
- (3) Includes the dismissal of four cases involving seven offenders in the total.

Please note that all decisions in administrative proceedings are public and available on BSM's website (in Portuguese)<sup>7</sup>.

<sup>7</sup> [www.bsm-autorregulacao.com.br](http://www.bsm-autorregulacao.com.br) (menu Atividades disciplinares e processos/ Consulte os processos).

## ADMINISTRATIVE PROCEEDINGS – 2017 HIGHLIGHTS

One of the highlights among the PADs that were completed in 2017 was PAD 15/2016, instituted in response to transactions in the period of July 27, 2015 to February 29, 2016, in which spoofing was identified in 1,123 situations.

Spoofing is a form of market manipulation that involves the creation of artificial conditions of supply and demand whereby the 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.

In this regard, responsibility was ascertained in the case of a B3 Participant and its Director in the implementation of controls to prevent, identify and stop abusive practices such as spoofing, due to trades brokered by this Participant in the name of two investors, of whom one was an institution belonging to the same business group as the Participant.

The PAD was concluded through a consent order that totaled R\$ 450,000.00 that the Participant and its Director paid to BSM.

Another noteworthy case was PAD nº 46/2016, which was concluded via a consent order totaling R\$ 1,600,000.00. In these proceedings responsibility was ascertained of a B3 Participant, its Director and a trader, for trades with the JSLG3 security that were executed to reach the target price stipulated by the Participant's customer, which was an issuer of equities listed on the exchange market operated by B3 and which executed a share repurchase program. This manipulation caused the price of JSLG3 to rise from R\$ 11.06 (closing

price of the December 22, 2014 trading session) to R\$ 12.75 (closing price of the December 30, 2014 trading session).

Another proceeding of note that was concluded in 2017 was PAD nº 35/2016, which ascertained the responsibility of a B3 Participant in the period between April 01, 2013 and June 30, 2014 for churning through the execution of excessive trades in the name of seven customers, seeking to generate revenues (brokerage fees and commissions) for the intermediary. This practice was identified due to the (a) absence of customer orders, (b) turnover rate in the period (portfolio turnover) and the (c) cost-equity rate in the period.

This PAD had its origins in MRP nº 121/2013 and in a special BSM audit of the Participant.

The PAD was concluded through a consent order in which the Participant undertook to: (1) refund the amount received as brokerage fees, taking into consideration the following premises: (a) refunding the investors by the amount lost, corresponding to the net result of the excessive transactions targeted by PAD 35/2016, corrected by the IPCA or by the index that substitutes it plus simple interest of 6% per annum, calculated on a daily pro rata basis from the date of the occurrence up until refund to the investors, and (b) payment to BSM of the difference between the brokerage fee received by the Participant (historical value) and the loss incurred by the investor (value of the loss) when the value of the loss is lower than the value of the brokerage fee paid, corrected by the IPCA or by the index that substitutes it, from the date that the loss occurs up until the date that payment is made to BSM, and (2) payment to BSM of the value corresponding to 20% of the total value of the brokerage fees received as a result of the excessive transactions targeted by PAD 35/2016, corrected by the IPCA or the index that substitutes it, from the date of the occurrence of the loss up until the date that payment is made.



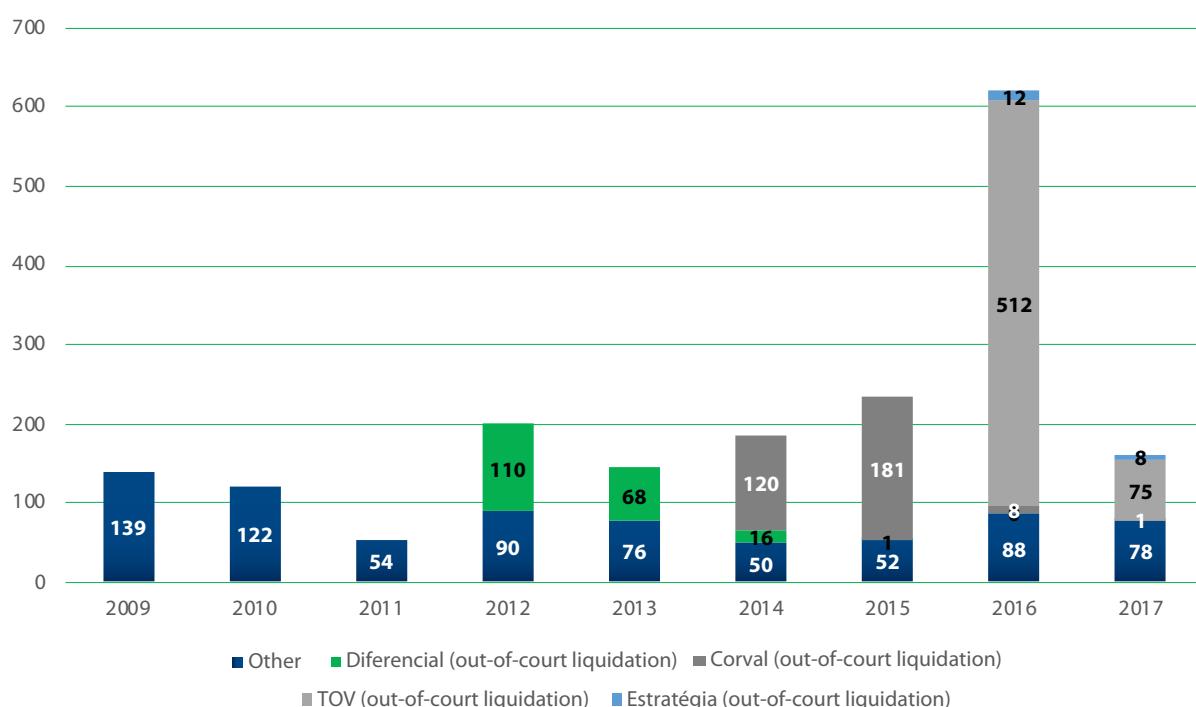
# **Investor Compensation Mechanism (MRP)**

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

of the exchange market operator in the intermediation of trades executed on the exchange or in custody services. BSM manages B3's Investor Compensation Mechanism (MRP) and is therefore responsible for managing the fund and ruling on compensation claims filed by investors<sup>8</sup>.

**Chart 3** 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 three brokerage houses (Diferencial, Corval and TOV) that were Participants accredited by B3 investors<sup>9</sup>.

Graph 3  
Claims made to the MRP



In 2017, BSM analyzed, commenced and finalized proceedings on the backlog of claims to the MRP from customers of TOV brokerage house in an average of 89 days. Since TOV's liquidation, 589 claims have been filed with the MRP.

At BSM there are two distinct procedural frameworks: (a) the MRP which consists of an investor protection mechanism in cases of losses caused by market Participants, as determined by the article 77 of CVM Instruction 461/2007, and (b) Administrative Disciplinary Proceedings, through which

<sup>8</sup> The status of claims filed and of BSM's rulings are available on the BSM webpage at [www.bsm-autorregulacao.com.br](http://www.bsm-autorregulacao.com.br) (menu MRP / Processos MRP).

<sup>9</sup> The Central Bank of Brazil ordered the out-of-court liquidation of Diferencial, Corval and TOV on August 09, 2012, September 11, 2014, and January 07, 2016, respectively.

there is analysis and judgment of the conduct of market Participants (and their administrators and agents) that breach rules that have been entrusted to BSM for inspection and, when pertinent, for imposition of the applicable penalties.

Regardless of the result of the MRP proceedings (accepted, denied or agreement between the Complainant and Offender) the BSM may adopt enforcement measures to deal with eventual irregularities committed by the Participant or its agents, identified in the MRP process.

Below we have highlighted three PADs that originated from irregularities identified in the procedural analysis of the MRP executed in 2017.

**Table 7** sets out the number of complaints received, concluded and ongoing since 2010. It is important to note that in 2017 BSM concluded 218 complaints, with the average period until conclusion of proceedings in 2017 reaching 146 days, compared to 213 days the year before. This average period is counted as of the date that BSM receives the complaint up until the date of the final decision within the scope of the BSM.

## MRP PROCEEDINGS– 2017 HIGHLIGHTS

### MRP PROCEEDING THAT ORIGINATED PAD 04/2017

PAD 04/2017 began with MRP Proceeding 476/2016. During the MRP Proceedings it was discovered that self-employed investment agents linked to the Brokerage House had provided information that led investors to believe the trades executed in B3's markets had a guaranteed financial return, with no or very little risk. In this way, self-employed investment agents were accused of failing to comply with the duty of acting in good faith when trading in the name of their customers, as foreseen in article 10 of CVM Instruction 497/2011.

### MRP THAT ORIGINATED PAD 12/2017

PAD 12/2017 began with MRP Proceedings 384/2016, 388/2016, 471/2016, 22/2017 and 111/2017. Within the scope of these proceedings, there was the identification of a recommendation made by an agent of the Participant for trades incompatible with the profile of the investors and a trading recommendation to a customer without a previously-defined investor profile, in infringement of item 1, sub-item 4, of the Basic Guidelines in effect from October 07, 2010 to July 16, 2015, article 5, subparagraphs I and II, of CVM Instruction 539/2013, in effect as of July 01, 2015, items 23.1 and 23.2 of the Basic Guidelines. In effect as of July 17, 2015, as well as article 30, heading, of CVM Instruction 505/2011.

### MRP PROCEEDING THAT ORIGINATED PAD 24/2017

PAD nº 24/2017 began as MRP 499/2016. During the MRP Proceedings there was the identification of a self-employed investment agent linked to the Brokerage House using a password and electronic signature, for exclusive use by the Complainants, to enter orders via the Home Broker electronic system. In this way, the self-employed investment agent was accused for having used the password and electronic signature, for exclusive use by the customer, to enter orders through the electronic system, as foreseen in article 13, subparagraph VII of CVM Instruction 497/2011.

Table 7  
Complaints Received, Concluded and in Progress

	2010	2011	2012	2013	2014	2015	2016	2017
Initial Caseload	212	222	187	228	240	252	110	173
Claims Received	122	54	200	144	186	234	620	162
Claims Concluded	112	89	159	132	174	376	557	218
<b>Final Caseload</b>	<b>222</b>	<b>187</b>	<b>228</b>	<b>240</b>	<b>252</b>	<b>110</b>	<b>173</b>	<b>117</b>

**Table 8** shows how many of these 218 claims concluded in 2017 were dismissed, denied or accepted. In 2017, BSM compensated investors whose claims were partially or totally accepted, to a total value of R\$ 2,665,900.18<sup>10</sup>.

Table 8  
BSM decisions in relation to Claims Made to the MRP

Decision	Nº.	%
Accepted (Totally or Partially)	104	48%
Claim Dismissed (No Grounds or Requirements not Met)	65	30%
Denied	31	14%
Under Appeal at CVM	6	3%
Agreement between Parties	12	6%
<b>Total</b>	<b>218</b>	<b>100%</b>

Tabela 9  
Total Amount of Compensation Paid by the MRP

MRP Compensation Paid	2011	2012	2013	2014	2015	2016	2017	Total
Brokerage houses under out-of-court liquidation	-	-	293.30	542.20	4,367.90	6,841.90	2,149.75	14,195.05
Other brokerage houses	417.00	1,354.90	145.00	594.20	538.40	377.70	516.15	3,943.35
<b>Total</b>	<b>417.00</b>	<b>1,354.90</b>	<b>438.30</b>	<b>1,136.40</b>	<b>4,906.30</b>	<b>7,219.60</b>	<b>2,665.90</b>	<b>18,138.40</b>

<sup>10</sup> 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	▲ 405.4	8.6350	8.6350	+0.10
	▲ 34.7080	▲ 0.7540	540.5	0.7540	▲ 054.0	8.7860	8.7860	
					▲ 405.4	8.6350	8.6350	
Global Stocks	<b>EWPE</b>	<b>-WEF</b>	<b>EFF</b>	<b>-WEF</b>	<b>EFF</b>	<b>-WEF</b>	<b>-WEF</b>	
\$ 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								
\$ 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	

# Notices to COAF

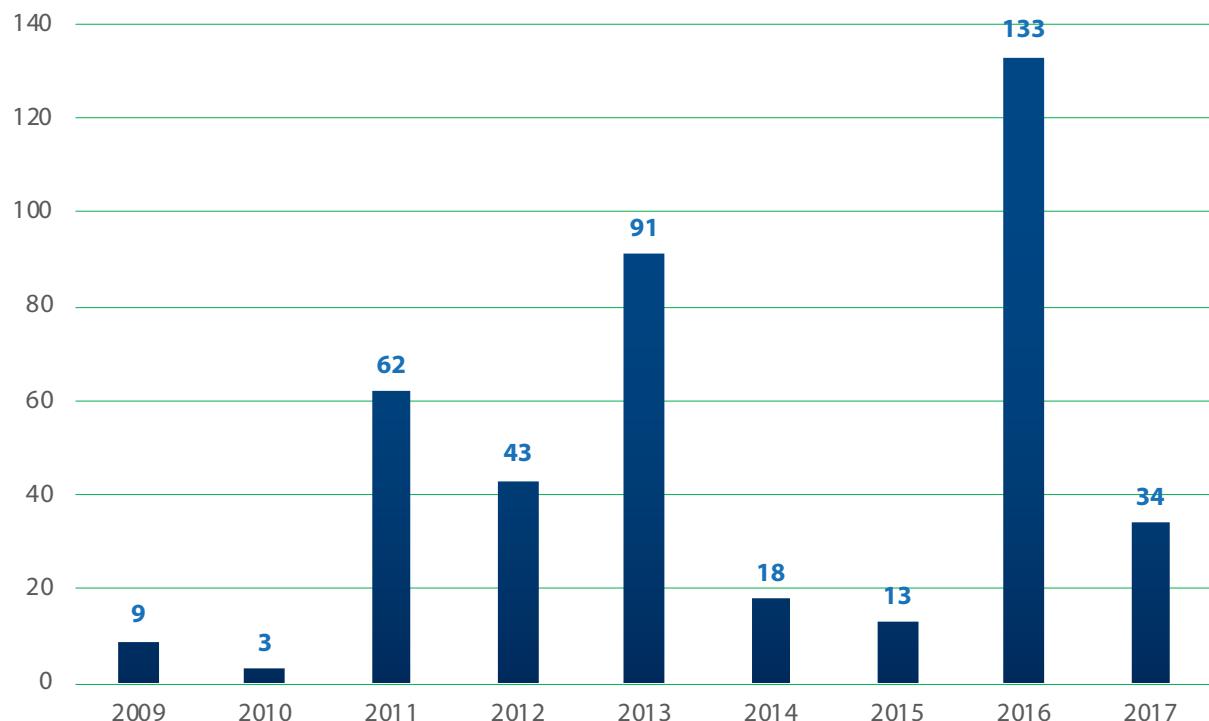
Law 9613/1998 and CVM Instruction 301/1999 require brokerage houses and other intermediaries, custodians, fund managers and other individuals or legal entities involved in certain activities to keep an up-to-date customer register and monitor customer transactions continuously, paying special attention 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 2017, BSM filed 34 such notices with COAF.

BSM also works with B3'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.

Graph 4  
BSM Notices to COAF



# Institutional Relations and International Insertion

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

In addition to this, BSM 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, for regulation and best practices for qualified capital market services, and for regulation and best practices for financial instrument trading. It also interacts with 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 special committees in these organizations, such as IOSCO's Affiliate Members Consultative Committee (IOSCO AMCC). Affiliate members of IOSCO include other self-regulatory organizations and international associations.

In 2017, in its international capacity, BSM took part in the Annual Conference of IOSCO AMCC in Mumbai, India. The conference was held over September 25-28 and BSM hosted panel sessions about its Work Plan, its work tools and cases of Spoofing and Layering.

Seeking to maintain a close relationship with the agents comprising the Brazilian market, BSM has hosted events about issues of interest, most notably workshops to guide market Participants in regard to special matters – mainly Money Laundering Prevention (PLD).

The main topics addressed in 2017 were the 2018 Audit Plan, as all CETIP UTVm Participants will be encompassed by it, and a discussion about BSM's expectations of compliance with the normative basis.



# Education and Training

BSM's senior 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 2017, nine employees received this benefit.

BSM also encourages its 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. In 2017, two employees were sent to the US for training in SAS statistical software analysis.

BSM also brings in experts from other countries to give courses to its staff and has held international seminars on relevant topics at its offices since 2011. The 2017 seminar was named "Market Structures and Rules to Resolve Conflicts of Interest, Front Running, Order Processing and Best Execution." Issues such as Spoofing and Layering, Data Mining and Cyber Security were also discussed. There were guest speakers from the Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA), as well as an expert in SAS software data mining and representatives of the market surveillance area of NASDAQ Nordics.

Almost 100 people took part in the training session, comprised of BSM and B3 employees alongside guests from the CVM, Central Bank of Brazil and ANBIMA.

BSM representatives also participate as speakers in B3's Educational Institute, in the TOP Programa geared to professors to disseminate knowledge about capital markets, and the Regulators Program for representatives of public and private regulatory and self-regulatory organizations.



# Administrative Activities

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

To this end, BSM has a four-person team dedicated to these activities. The main tasks of the administrative support area 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 10** summarizes the key statistics for these activities

Table 10

Activity	Total 2017	Monthly Average
Correspondence Items Sent	4,918	410
Correspondence Items Received	2,369	197
Document Digitizing (No. of pages)	137,957	11,496
Processing of Receipts (travel expenses, taxis, etc.)	1,084	90
Flight and Hotel Bookings	1,277	94

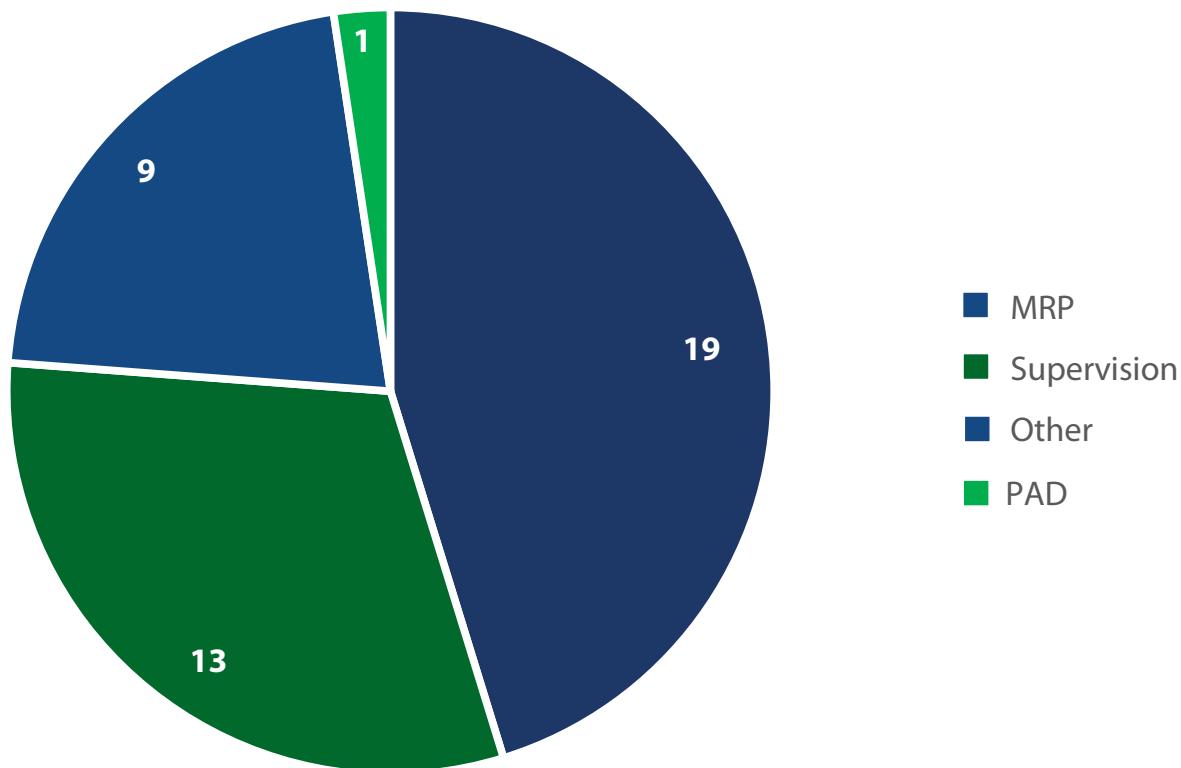
A photograph showing a row of computer monitors in what appears to be a call center or customer service environment. Each monitor is mounted on a stand with a microphone boom arm. A headset is resting on the rightmost monitor. In front of the monitors, there are several keyboards and mice. The scene is lit with a blue tint.

# Public Information Service (SAP)

B3 and BSM maintain a Public Information Service to receive requests for information, criticisms, and suggestions regarding the activities of BSM, B3 and its Participants. The service is available by phone, by filling out a specific form on BSM's website or in person at BSM's head office.

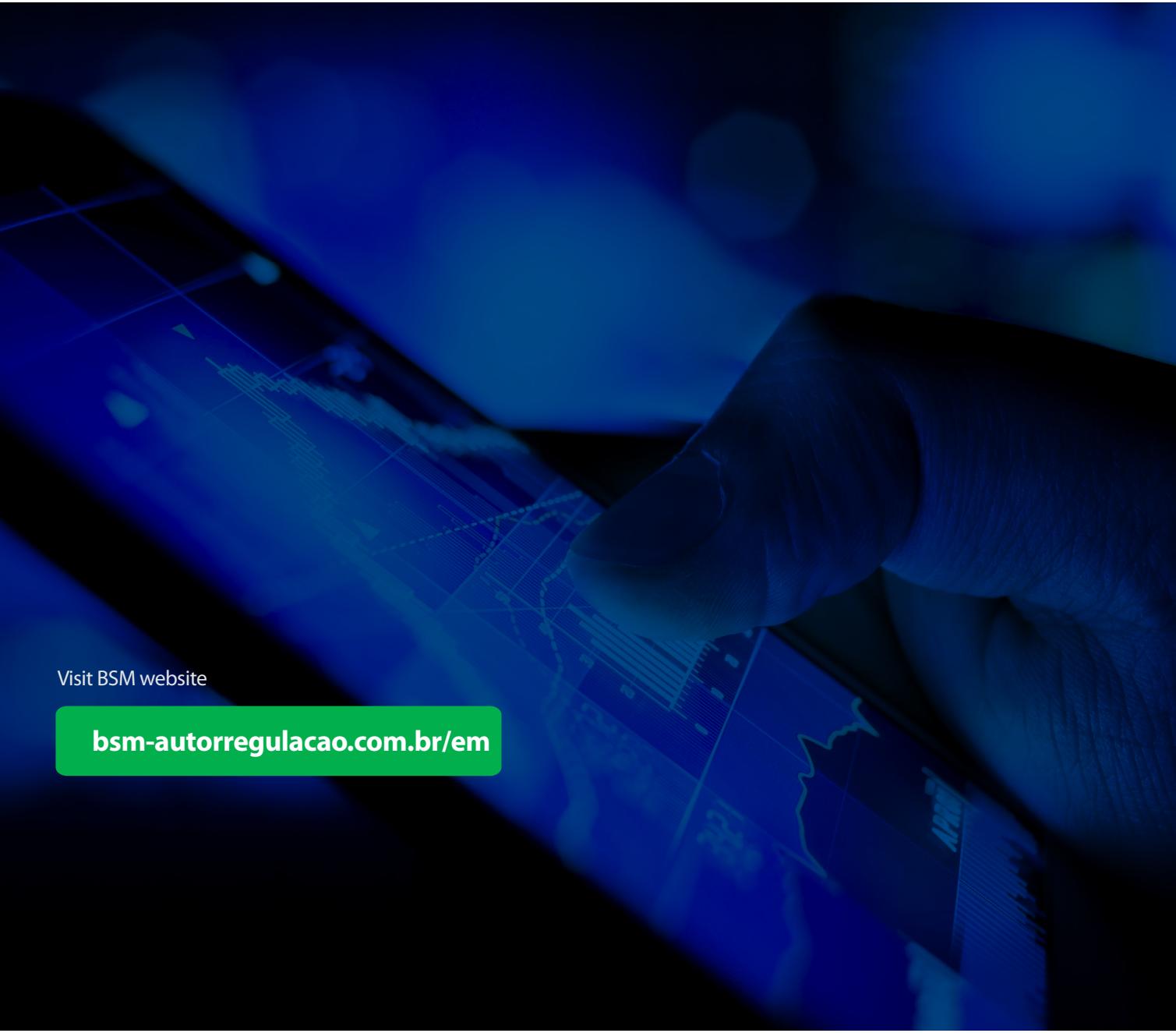
In 2017, BSM received 42 enquiries. **Chart 5** shows the main subjects of these enquiries.

Chart 5  
Public Information Service (SAP) – Main types of enquiries



Most of the enquiries were related to complaints, generally investors wishing to know the behavior of certain equities





Visit BSM website

[bsm-autorregulacao.com.br/em](http://bsm-autorregulacao.com.br/em)

# BSM

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