August 14, 2020
2664/2020-DAR-BSM

EXTERNAL COMMUNICATION

To: B3's Market Participants – Listed Segment

Re: **Supervision of Intentional Self-Trading in Auctions**

On March 17, 2020, B3 S.A. – Brasil, Bolsa, Balcão ("B3") published Circular Letter 033/2020-PRE[1] about changes to its Trading Procedures Manual (MPO),[2] including a new procedure for dealing with intentional trades by the same investor in an auction (self-trading), and on June 30, 2020, B3 published Circular Letter 082/2020-PRE setting out the rules for monitoring of self-trades by the Electronic Trading Department (DNE).

The new procedure distinguishes between regular and irregular self-trades,[3] and establishes six months as the period for verification[4] of irregularities, including recurrent violations. B3, BSM and CVM are now jointly responsible for supervision of irregularities.

BSM will detect recurrent irregular self-trading by market professionals and investors in accordance with CVM Instruction CVM 8/79, I and II (a), and will take appropriate action.

Recurrence is deemed to refer to self-trades that are executed with the aim of intentionally relinquishing entered orders and that injure one or more investors who enter orders affected by the relinquishment. BSM will receive trades identified by B3 and will use this information in its analysis.

[1] http://www.b3.com.br/pt_br/regulacao/oficios-e-comunicados/oficios-e-comunicados/
[2] http://www.b3.com.br/pt_br/regulacao/estrutura-normativa/regulamentos-e-manuais/
[3] According to the MPO, self-trades are deemed regular if they are due to operating error or executed at the start of an auction, i.e. (a) in the first 60 (sixty) seconds in the case of securities and options referenced to equities, the Bovespa Index (Ibovespa), the Brazil-50 Index (IBrX-50) and ETFs, or (b) in the first 30 (thirty) seconds in the case of all other derivatives. The rest are deemed irregular.
[4] Verification periods correspond to the periods January-June and July-December in each calendar year.

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Section 1. Recurrence criteria for self-trades executed via trading desks

For self-trades executed via trading desks, BSM will open an investigation to have the participant conduct a conclusive analysis of such trades when more than three self-trades deemed irregular are performed by the same trader within a given verification period.

If a self-trade is executed after the investigation begins and in the same verification period, the participant and trader will be subject to a penalty unless they can prove the self-trade was unintentional.

BSM conducts monthly checks to detect possible irregularities, notifying those concerned in the following month, as exemplified in Table 1.

Table 1. Example of supervisory flow for self-trades executed via trading desks

Cycle	Month	No. of self-trades	Cumulative	Action by BSM
	June			
1	July	-	-	
	August	2	2	
	September	2	4	
	October	-	4	Notification
	November	1	5	
	December		5	Penalty
2	January			

Legend:

Cycle: six-month verification period
Month: month in which self-trade is executed
No. of self-trades: number of self-trades executed per operator in the month
Cumulative: number of self-trades executed monthly in the six-month period
Action by BSM: measures taken by BSM, consisting of:

1) Notification: Determines suspension of the practice as of the day on which notice is received and requires the participant to convey its purport to traders;
2) Penalty: sanction applied to the participant and trader via an administrative proceeding.

As the example shows, BSM always serves notice in the month following verification and opens a penalty proceeding if another irregular self-trade occurs after notice is served.

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The response required from the trader is to cease and desist from the violation.[5] The participant is required to:

1) Inform all traders of the notice;
2) Monitor all self-trading notifications sent by B3's Electronic Trading Department (DNE);
3) Notify the traders responsible for irregular self-trades in auctions and warn them of the effects of recurrence;
4) Determine that traders cease and desist from the violation;
5) Inform all traders of the irregular self-trades executed in the verification period.[6]

The decision tree based on participant responses and BSM's analysis is presented in Annex I.

Section 2. Recurrence criteria for self-trades executed by investors via DMA sessions

For self-trades executed via DMA sessions, when a customer (investor) exceeds three irregular self-trades BSM opens an investigation to have the participant conduct a conclusive analysis of the trades concerned.

In the event of recurrence during the verification period, BSM opens another investigation. Another self-trade after the second notice (or determination) subjects the participant to a penalty.

BSM conducts monthly checks to detect possible irregularities, notifying those concerned in the following month, as exemplified in Table 2.

[5] The practice is a violation of CVM Instruction 8/79, I and II, (a) ("creation of artificial conditions").
[6] Continuation of the practice is a violation of CVM Instruction 505/11, article 32 ("supervisory failure").

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Table 2. Example of supervisory flow for self-trades executed by investors via DMA

Cycle	Month	No. of self-trades	Cumulative	Action by BSM
	June			
1	July	-	-	
	August	4	4	
	September	1	5	Notification
	October	-	5	Notification
	November	1	6	
	December		6	Penalty
2	January			

Legend:

Cycle: six-month verification period
Month: month in which self-trade is executed
No. of self-trades: number of self-trades executed per investor in the month
Cumulative: number of self-trades executed monthly in the six-month period
Action by BSM: measures taken by BSM, consisting of:

1) Notification: Determines suspension of the practice as of the day on which notice is received and requires the participant to convey its purport to investors;
2) Penalty: sanction applied to the participant via an administrative proceeding.

The participant is required to:

1) Monitor all self-trading notifications sent by B3's Electronic Trading Department (DNE);
2) Notify customers regarding irregular self-trades in auctions and warn them of the effects of recurrence;
3) Determine that customers cease and desist from the violation;
4) Inform all customers of the irregular self-trades executed in the verification period.[7]

The decision tree based on participant responses and BSM's analysis is presented in Annex II.

[7] Continuation of the practice is a violation of CVM Instruction 505/11, article 32 ("supervisory failure").

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Section 3. General Provisions

Participants must do everything possible to assure market integrity and prevent the continuation of violations of which they are aware, in accordance with item 126 of the Basic Script and CVM Instruction 505/2011, article 32 (I).

It is important to note that (i) payment of penalties does not waive the application of sanctions by BSM; (ii) self-trades deemed by BSM to appear to be fraudulent or part of an attempt to manipulate prices are not covered by the rules set out in Sections 1 and 2; (iii) all self-trades are reported to CVM for analysis in accordance with its own criteria.

In light of B3's Circular Letter 033/2020-PRE, dated March 17, 2020, the weekly notices issued by DNE on self-trades in auctions, and the present communication, the alerts regarding self-trades in auctions shared by BSM will be replaced by the new joint routine with B3.

Further clarification can be obtained from BSM by calling +55 11 2565-6871/6074/6144 or emailing bsm@bsmsupervisao.com.br, and by visiting https://www.bsmsupervisao.com.br to watch a webinar held on August 11, 2020, to present the new B3/BSM supervisory routine.

BSM is available to assist participants with education of customers and their legal representatives.

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ANNEX I. Decisions on self-trades via trading desks

1st Notification		2nd Notification
Violation	**BSM's analysis – first alert**	**BSM's analysis – recurrence**
Trader (Violation ICVM 8 "a")	Is the trader's justification for the self-trade accepted? **Yes –** Case dismissed **No –** Warning not to repeat irregular practice	Is the trader's justification for the self-trade accepted? **Yes –** Case dismissed **No – Administrative proceeding**
Trades in own portfolio accounts (Violation ICVM 8 "a")	Is the justification for the self-trade accepted? **Yes –** Case dismissed **No** – Warning not to repeat irregular practice	Is the justification for the self-trade accepted? **Yes –** Case dismissed **No – Administrative proceeding**
Participant (Violation CVM Instr. 505/2011, art. 32)	Is the participant's justification for the self-trade accepted? **Yes –** Case dismissed **No** – Warning not to repeat irregular practice	Is the participant's justification for the self-trade accepted? **Yes –** Case dismissed **No – Administrative proceeding**

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ANNEX II. Decisions on self-trades via DMA

1st Notification		2nd Notification	3rd Notification
Violation	**BSM's analysis – first alert**	**BSM's analysis - recurrence**	
Customer (Violation ICVM 8 "a")	Is the customer's justification for the self-trade accepted? **Yes –** Case dismissed **No –** Case forwarded to CVM	Is the customer's justification for the self-trade accepted? **Yes –** Case dismissed **No –** Case forwarded to CVM	Is the customer's justification for the self-trade accepted? **Yes –** Case dismissed **No – Case forwarded to CVM**
Trades in own portfolio accounts (Violation ICVM 8 "a")	Is the justification for the self-trade accepted? **Yes –** Case dismissed **No** – Warning not to repeat irregular practice	Is the justification for the self-trade accepted? **Yes –** Case dismissed **No – Administrative proceeding**	
Participant (Violation CVM Instr. 505/2011, art. 32)	Is the participant's justification for the self-trade accepted? **Yes –** Case dismissed **No** – Warning not to repeat irregular practice	Is the participant's justification for the self-trade accepted? **Yes –** Case dismissed **No** – Warning not to repeat irregular practice	Is the participant's justification for the self-trade accepted? **Yes –** Case dismissed **No – Administrative proceeding**

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