

History, intention and effect

Market Manipulation in Australia

BFSLA Conference – 2 September 2017
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Outline

1. Refresher on provisions
2. Interaction with Commonwealth Criminal Code
3. An “artificial” price
4. The role of intention
5. Effect / likely effect
6. Market manipulation outside equities / futures

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Market manipulation

Section 1041A

A person must not take part in, or carry out (whether directly or indirectly and whether in this jurisdiction or elsewhere):

(a) a transaction that has or is likely to have; or

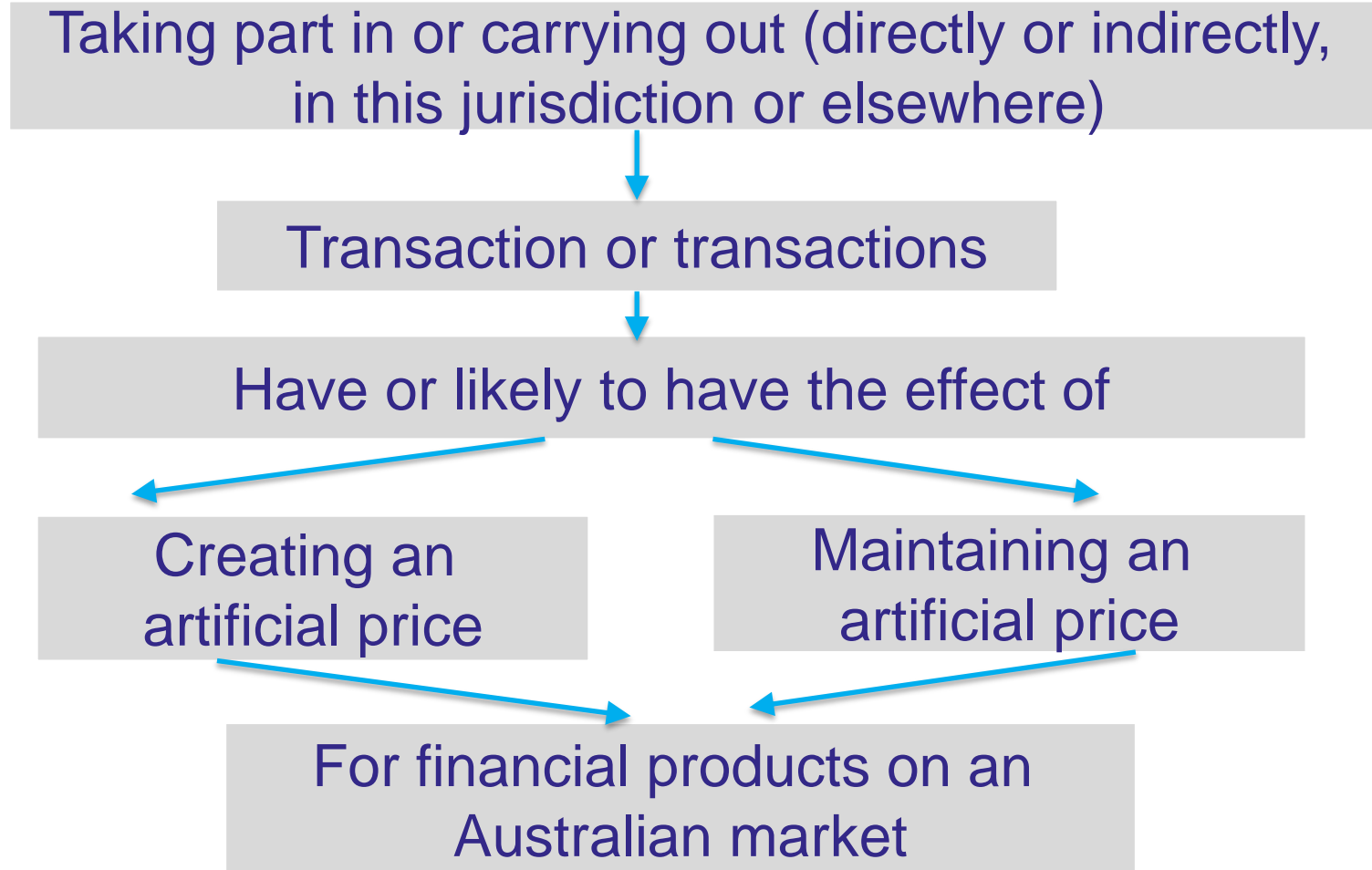
(b) 2 or more transactions that have or are likely to have;

the effect of

*(c) creating an **artificial price** for trading in financial products on a financial market operated in this jurisdiction; or*

(d) maintaining at a level that is artificial (whether or not it was previously artificial) a price for trading in financial products on a financial market operated in this jurisdiction.

Elements of Market Manipulation



Market manipulation

Section 1041B

(1) A person must not do, or omit to do, an act (whether in this jurisdiction or elsewhere) if that act or omission has or is likely to have the effect of creating, or causing the creation of, a false or misleading appearance:

(a) of active trading in financial products on a financial market operated in this jurisdiction; or

(b) with respect to the market for, or the price for trading in, financial products on a financial market operated in this jurisdiction.

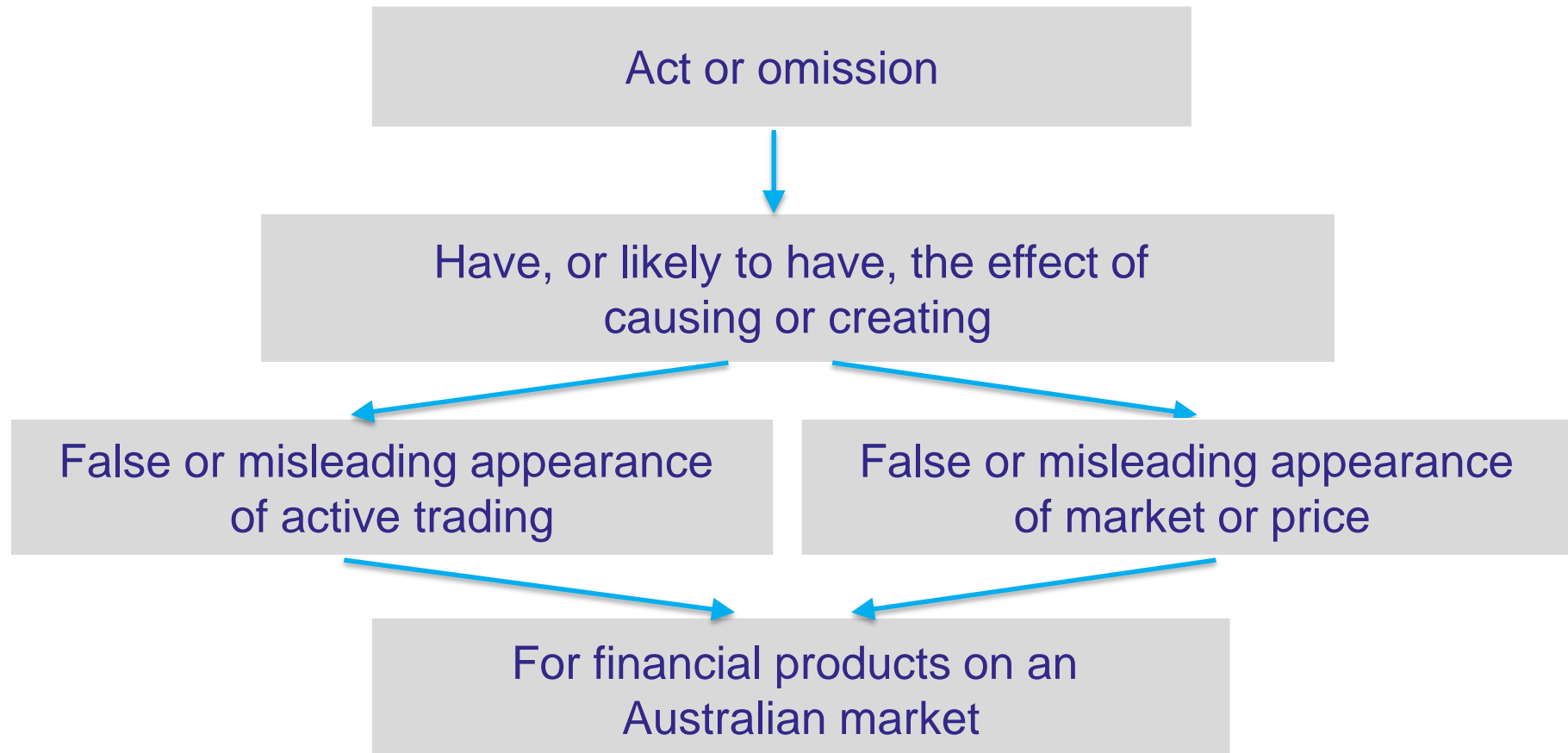
Section 1041C

(1) A person must not (whether in this jurisdiction or elsewhere) enter into, or engage in, a fictitious or artificial transaction or device if that transaction or device results in:

(a) the price for trading in financial products on a financial market operated in this jurisdiction being maintained, inflated or depressed; or

(b) fluctuations in the price for trading in financial products on a financial market operated in this jurisdiction.

Elements of false trading and market rigging



Market manipulation

“[p]erhaps the most polite thing to say about these provisions is that they do not appear to have been included in the [Corporations] Act as a result of careful consideration of policy objectives. Moreover, there are significant overlaps and inconsistencies of style between the provisions reflecting the fact that the sections have quite different origins and have been added together in this part with little attention given to ensuring their practical combined operation.”

-Professor Ann O’Connell, Melbourne Law School

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Interaction with Commonwealth Criminal Code

Does Chapter 2 of the Commonwealth Criminal Code apply to the market manipulation provisions in the case of a civil penalty proceeding?

Obiter from Rares J (Dowsett and Gleeson JJA agreeing) in *Gore v Australian Securities and Investments Commission* [2017] 341 ALR 189 implying that it does, because the same provisions can give rise to both civil and criminal liability.

Considered recently in *Australian Securities and Investments Commission v Whitebox Trading Pty Ltd* [2017] FCAFC 100

Interaction with Commonwealth Criminal Code

“To conclude that Gore is correct on this issue would inevitably lead to an affirmative answer to the separate question, such that Chapter 2 of the Criminal Code would apply to these civil proceedings concerning ss 1041A and 1041B. That in turn would mean that, in order to establish the alleged contraventions and obtain the declaratory and pecuniary penalty relief sought, ASIC would not only have to prove that the contraventions had in fact taken place in the sense of proving, on the balance of probabilities, that the conduct proscribed by each of ss 1041A and 1041B of the Corporations Act had taken place in the designated circumstances or with the designated results. ASIC would also have to prove criminal fault elements derived from Chapter 2 of the Criminal Code for each of the proscribed physical elements, rather than any state of mind as may be drawn from the terms of those two provisions. Such express statutory fault elements would be imposed by the operation of s 5.6 of the Criminal Code in relation to s 1041A, and by the operation of s 1041B(1A) in relation to s 1041B(1).”

Interaction with Commonwealth Criminal Code

“In expanding the number of civil penalty provisions, the legislature evidently made a deliberate choice to maintain separate norms which constituted most of the civil penalty provisions and upon which most of the criminal offence provisions were based, and to make the market manipulation proscriptions also civil penalty provisions.”

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An “artificial” price

Mason J in *North v Marra Developments Limited* (1981) 148 CLR 42:

“It is not altogether easy to translate the generality of this language into a specific prohibition against injurious activity, whilst at the same time leaving people free to engage in legitimate commercial activity which will have an effect on the market and on the price of securities. ...

*The section seeks to ensure that the market reflects the forces of genuine supply and demand. By “**genuine supply and demand**” I exclude buyers and sellers whose transactions are undertaken for the sole or primary purpose of setting or maintaining the market price.”*

An “artificial” price

High Court in *DDP v JM* (2013) 250 CLR 135:

*“The fundamental point ...is that market manipulation is centrally concerned with conduct, intentionally engaged in, which has resulted in a price which does not reflect the **forces of supply and demand**...”*

*The forces of ‘genuine supply and demand’ are those forces which are created in a market by buyers whose purpose is to **acquire at the lowest available price and sellers whose purpose is to sell at the highest realisable price.**”*

An “artificial” price

Goldberg J in *ASIC v Soust* [2010] FCA 68:

“The fundamental issue to address is what is meant by an ‘artificial price’. The expression ‘artificial price’ is defined in the Shorter Oxford English Dictionary as ‘constructed, contrived’, ‘not natural though real’ and ‘not real’...

*connotes a price created not for the purpose of implementing or consummating a transaction between genuine parties wishing to buy and sell securities, but rather for a purpose unrelated to achieving the outcome of the interplay of **genuine market forces of supply and demand...***

*fundamental to the working of the free market forces of securities exchanges such as the ASX that buyers are concerned to **buy securities at the lowest possible price and sellers are concerned to achieve the highest possible price***

An “artificial” price

Gleeson CJ, with whom Powell JA agreed, in *Fame Decorator Agencies Pty Ltd v Jeffries Industries Ltd* (1998) 28 ACSR 58:

*“a price reflecting **basic forces of supply and demand** working in an open, efficient and well-informed market, is contrasted with an artificial price resulting from manipulative conduct”*

Dowsett J, *Australian Securities and Investment Commission v Administrative Appeals Tribunal* (2010) 187 FCR 334

*“potentially misleading effect of market transactions which are **not between a buyer and a seller who are both seeking the most favourable price**”*

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The role of intention

- No mention of intention anywhere in the current market manipulation provisions
- Contra the provisions prior to 2002
- But see Court in JM:

“The price that results from a transaction in which one party has the sole or dominant purpose of setting or maintaining the price at a particular level is not a price which reflects the forces of genuine supply and demand ...If the offer results in a transaction, that is a transaction which can be characterised as at least likely to have the effect of creating or maintaining an artificial price for trading in the shares.”

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Effect / likely effect

- In s 1041A itself, there is no requirement for contravention of any intention of creating or maintaining an artificial price
- Contravention without intention?
- “The fat finger error”
- The innocent counterparty?

Effect / likely effect

- Dowsett J, *Australian Securities and Investment Commission v Administrative Appeals Tribunal* (2010) 187 FCR 334 at [49]:
- *“In attacking participation in transactions which have a particular effect or likely effect, s 1041A goes well beyond the reach of s 70. However there is nothing unusual about such an approach. Provisions in the Trade Practices Act 1974 (Cth) take a similar approach. In the criminal law, offences are not infrequently defined by reference to the effect or likely effect of conduct. It may seem that s 1041A offers little guidance as to what is lawful and what is not. However that perception is misconceived. Involvement in any transaction in which both the buyer and seller seek the most advantageous price will not engage s 1041A. Involvement in any other transaction may do so. It is, of course, possible that one party will be a bona fide purchaser or seller and the other, not. **Insofar as concerns proceedings for civil penalties, s 1317S will protect innocent parties.** It is probable that in criminal proceedings, absence of knowing involvement will be an answer to any charge.”*

Effect / likely effect

Section 1317S(2) of the Corporations Act is a slip rule which provides:

“(2) If:

(a) eligible proceedings are brought against a person; and

(b) in the proceedings it appears to the court that the person has, or may have, contravened a civil penalty provision but that:

(i) the person has acted honestly; and

(ii) having regard to all the circumstances of the case (including, where applicable, those connected with the person's appointment as an officer, or employment as an employee, of a corporation or of a Part 5.7 body), the person ought fairly to be excused for the contravention;

the court may relieve the person either wholly or partly from a liability to which the person would otherwise be subject, or that might otherwise be imposed on the person, because of the contravention.”

Effect / likely effect

- **Possible indirect effect?**
- A transaction giving rise to an “artificial price” in a financial market does not necessary have to occur on the financial market in question.
- It is possible that transactions in other products have, or are likely to have, an indirect effect on a financial market for other products.
- For example, current BBSW proceedings brought by ASIC

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Non-equities / futures markets

- Case law in Australia has almost exclusively focused on market manipulation in the context of listed securities.
- Court in JM at [58]:
 - “*It is important, however, to emphasise that this case concerns on-market transactions in shares listed on the ASX, and that the discussion which follows is confined to transactions of that kind.*”
- Securities and futures markets tend to share a number of features that are not necessarily common to markets outside this context:
 - Low barriers to entry;
 - Large number of participants;
 - Low sophistication of participants; and
 - Active management and monitoring by market operators