



ASIC

Australian Securities & Investments Commission

REPORT 425

ASIC supervision of markets and participants: July to December 2014

March 2015

About this report

This report summarises key outcomes of ASIC's market and participant supervisory and surveillance functions and highlights markets-related enforcement outcomes for the period 1 July to 31 December 2014.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Previous reports on ASIC supervision of markets and participants

Report number	Report date
REP 405	August 2014
REP 386	March 2014
REP 366	August 2013
REP 327	February 2013
REP 296	August 2012
REP 277	February 2012
REP 243	July 2011
REP 227	January 2011

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Overview

ASIC supervision of markets and participants

- 1 The Australian Securities and Investments Commission (ASIC) is Australia's corporate, market and financial services regulator. As market regulator, we are responsible for the supervision of trading on Australia's domestic licensed equity, derivatives and futures markets.
- 2 Financial markets play a central role in the growth and prosperity of our economy by facilitating the raising of capital and the efficient allocation of resources and risks by investors.
- 3 Our core priority is the promotion of investor confidence through fair and efficient markets. Crucial to the pursuit of this priority is market infrastructure that is robust, where trading, clearing and settlement of transactions is orderly and efficient, and where market misconduct is minimised.
- 4 We use a number of regulatory tools to pursue this priority. We conduct surveillance of listed equities, futures and options markets—and supervise compliance in those markets with the *Corporations Act 2001* (Corporations Act) and ASIC market integrity rules: see Section A. We also seek to ensure that market participants and securities dealers are meeting their Australian financial services (AFS) licence conditions: see Section B.
- 5 Where we detect potential market misconduct, we conduct investigations and may take enforcement action—which can result in severe penalties in appropriate cases: see Section C. The regulatory tool(s) we choose to use in response to a potential breach of the law will depend on the outcome that we are seeking to achieve. These outcomes include:
 - (a) deterrence;
 - (b) improved compliance;
 - (c) protection of the public;
 - (d) compensation for investors; and
 - (e) punishment.
- 6 We are committed to preventing inappropriate conduct and improving poor compliance practices before they affect the integrity of markets. We refer to this as achieving 'positive behavioural change'. Engagement with stakeholders (both formal and informal), education, guidance and warning letters are some of the tools we use to achieve positive behavioural change: see paragraphs 9–24.

Purpose and scope of this report

- 7 This report summarises key operational statistics and outcomes achieved by ASIC in relation to ASX, ASX 24 and Chi-X for the period 1 July to 31 December 2014. It is the ninth of ASIC's six-monthly market supervision reports. Previous reports are available on [our website](#).
- 8 This report also highlights markets-related enforcement outcomes which were achieved by ASIC during this period. A comprehensive account of our enforcement activities over this time is set out in Report 421 *ASIC Enforcement outcomes: July to December 2014* (REP 421).

Achieving positive behavioural change

- 9 Achieving positive behavioural change is crucial to our work as market regulator. Early intervention allows for the prevention of potential breaches, and consequential investor losses, before they occur.
- 10 The types of conduct we target for positive behavioural change are activities that, without regulatory intervention, could result in a breach of the Corporations Act or market integrity rules. For example, poor information-handling processes may enable leakage of confidential information, which may facilitate insider trading.
- 11 Conduct that has already developed into a suspected breach may not be a suitable candidate for activities designed to achieve positive behavioural change but may be subject to ASIC enforcement action.
- 12 We use a number of techniques to achieve positive behavioural change. In particular, we consider direct engagement with market participants to be a highly-effective method for changing behaviour and improving practices.

Example 1: Wash trades

In 2012, we noticed that high-frequency trading was generating an unacceptable level of wash trades (i.e. trades with no change in beneficial ownership) and trade cancellations. The extent of this was affecting value-weighted average prices which are used for many other trading purposes.

We encouraged a change in behaviour through a campaign involving industry presentations and targeted meetings. Industry responded positively and wash trades are no longer a significant issue. It should be noted that market operators assisted in devising methods to avoid wash trades.

Direct engagement

- 13 We maintain an active dialogue with market participants to address compliance concerns. For example, between 1 July and 31 December 2014,

discussions with market participants led to the amendment of order execution methods and the review of trading algorithms on 26 occasions: see Table 4.

- 14 Our market surveillance activities sometimes reveal unusual trading patterns which may be indicative of potential market misconduct. As part of our early-engagement process, we work with market participants (including fund managers, hedge funds and individual traders) to raise our concerns about such behaviour: see Example 2.

Example 2: Working with participants to improve controls

A contract-for-difference (CFD) provider recently removed a number of penny stocks from its products list so that its clients could no longer trade those stocks through the firm. This makes it more difficult for those engaged in account-hacking activities through other market participants to yield profits, because the shares involved in hacking are often penny stocks which are thinly traded under normal market conditions and easier to manipulate.

The CFD provider will also report to ASIC any instances of suspicious trades made by clients who have made significant profits in a short period of time (as compared to their initial investment outlay), and where the trades do not appear to be the result of publicly-available information.

Assessments of participants

- 15 In the relevant period we began conducting compliance liaison meetings. We expect to complete one meeting with each market participant each calendar year (there are approximately 130–140 market participants). These meetings focus on gathering intelligence for information and assessment purposes, raising market participants' awareness of their obligations, and highlighting ASIC's current areas of focus.
- 16 During each meeting, a series of questions are asked about key risks to the business and industry—providing crucial insight into what the current issues of the day are, as well as monitoring trends.
- 17 We also conduct risk assessment detection and response (RADAR) visits. These visits provide the same benefits as our compliance liaison meetings, with an additional assessment of the risks associated with each market participant's business.
- 18 After conducting a risk assessment, we may send the market participant a letter containing our observations and recommendations, which can include suggestions for improving compliance where concerns have been identified. This can lead to improvements in market participants' compliance frameworks and an increased awareness of their compliance obligations.
- 19 ASIC utilises the information gathered from compliance liaison meetings and RADAR visits, along with other intelligence, to identify key risk areas

or concerns in the market. Based on this information and other intelligence, we conduct compliance reviews (both thematic and specific to a single firm) which can be targeted or general in nature. The compliance reviews aim to obtain and analyse more detailed information about these key risks or, in some instances, suspected misconduct by participants.

- 20 After conducting a compliance review we will normally send a letter containing our observations and recommendations—this letter can include suggestions for improvements and lead to behavioural changes and disruption to potential misconduct. We also intend to inform and educate the wider market on the key trends and risks that we have identified. We also promote good practices that have been adopted by some firms, and which should be considered by other firms more broadly.
- 21 By undertaking this risk-based approach to the assessment of market participants we are able to obtain timely information about current and future trends, and key risks to markets—allowing us to focus attention on the key risks we have identified.

Warning letters

- 22 Warning letters provide ASIC with an alternative approach to enforcement action by communicating regulatory concerns and ensuring they are received by the individuals or entities involved. During the relevant period, we issued 12 warning letters to market participants for markets or compliance-related issues.
- 23 Warning letters may be relied on by ASIC as an aggravating factor at the Markets Disciplinary Panel (MDP) if the behaviour continues and enforcement action is commenced: see Example 2 in Report 405 *ASIC supervision of markets and participants: January to June 2014* (REP 405).

Industry publications

- 24 We continue to publish a monthly ASIC Market Supervision Update (MSU) highlighting current issues in market supervision and surveillance, including changes to market integrity rules and compliance issues. We also contribute to a number of external publications, including the Stockbrokers Association of Australia newsletter. These publications enable us to inform industry about issues of current concern to ASIC.

Note: You can subscribe to the MSU, or access previous issues, [on our website](#).

Significant outcomes for the relevant period

Market surveillance

- 25 In the relevant period, we conducted a total of 112 market surveillance enquiries of equities and futures participants, including reactive, proactive and targeted surveillances.
- 26 We continue to enhance the functionality of our new market surveillance system, Market Analysis and Intelligence (MAI). The flexibility of the system has allowed ASIC to implement a Rapid Application Development process to design and implement new alert and report functionality for MAI in very short periods of time, compared to traditional software development processes. In early-2014, we developed a new insider trading report in MAI, looking at ASX equities and derivatives data in far greater detail than the previous system allowed for. In the second half of 2014, we also created a new market manipulation report to more efficiently analyse large volumes of trading data.

Example 3: Improved functionality and reporting

The improved surveillance capabilities of MAI assisted with identifying a persistent pinging strategy in an ASX20 security trading in ASX Centre Point and Chi-X hidden public dark venues. Pinging is the practice of using the placement of very small orders to test if there is liquidity.

Key traders suspected of possibly breaching Rule 5.7.2 of the ASIC Market Integrity Rules (ASX Market) 2010 (and negatively impacting market quality) were identified. After further discussions with the market participants and end clients, the behaviour ceased. The unwanted cost imposition on users of these public dark venues has been sufficiently addressed and, as a result of our continued engagement with participants and the market operator, we have improved market efficiency and integrity of public dark venues.

Note: See Section A for further details of our surveillance activities (including MAI).

Supervision of market participants

- 27 In the relevant period, we carried out 55 market participant compliance reviews. In our reviews, we noted that there were some shortcomings in the monitoring and supervision of representatives due to non-compliance with procedures, insufficient resources or a lack of oversight in regional or branch offices.
- 28 In addition, we completed six risk-based assessment visits. As a result of these assessments, we recommended that one market participant review and enhance its supervisory arrangements, taking into consideration the nature, scale and geographical distribution of its business.

Note: See Section B for further details of our supervision activities.

Market enforcement outcomes

- 29 In the relevant period, our Market Integrity Enforcement team achieved a total of 15 significant enforcement outcomes. As shown in Table 1, individual enforcement outcomes may achieve multiple regulatory objectives.

Table 1: Objectives of enforcement action

Enforcement action (no. of actions in the relevant period)	Objective of enforcement action			
	Punishment	Improved compliance	Protection of the public	Deterrence
Insider trading (3)	✓	✓	✓	✓
Market manipulation (2)	✓	✓	✓	✓
Infringement notices (8)	✓	✓	✓	✓
Pecuniary penalties (2)	✓	✓	✓	✓

- 30 The Market Integrity Enforcement team typically had over 85 matters under investigation at any one time during the relevant period.
- 31 Appropriate handling of confidential information remains essential to ensuring all investors are trading on the same information. We continue to consider company briefings to market participants (including their research analysts) and investors to be a significant risk area for selective disclosure of confidential, price-sensitive information.
- 32 A significant enforcement outcome for ASIC was the sentencing of former Genetic Technologies Ltd (GTG) Chief Executive, Dr Mervyn Jacobson, to a total of two years and eight months, after he was convicted of manipulating the share price of GTG.
- 33 ASIC, with the cooperation of the Australian Federal Police, also successfully extradited Hui Xiao—the former Managing Director of Hanlong Mining Investment Pty Ltd—and charged him with 104 counts of insider trading. Further details of our markets enforcement outcomes can be found in Section C.

Future areas of focus

Market Entity Compliance System

- 34 With the MAI surveillance system rolled out, attention has turned to one of the next deliverables of the Flexible Advanced Surveillance Technologies (FAST) project, the Market Entity Compliance System (MECS). MECS is intended to enhance the way market participants and operators interact with ASIC.

- 35 MECS is a web portal that will make regulatory compliance easier by enabling easy, electronic submission and monitoring of notifications and applications, with outcomes recorded for future reference. An automatic reminder service will alert market participants and operators of upcoming compliance deadlines. These features will support market participants and operators in fulfilling their regulatory obligations and enhance their communication with ASIC, delivering benefits to industry.
- 36 For example, market participants and operators will be able to access and manage their own organisational information (e.g. contact information and website details) and people (e.g. organisational roles and MECS users) within MECS. For the first time, market participants will be able to view lists of regulatory roles relevant to their organisation, such as accredited derivatives advisers (ADAs) and responsible executives, enhancing communication between ASIC, market participants and operators.

Confidential information

- 37 ASIC is eager to raise industry standards in relation to the treatment of confidential information by listed companies. We are undertaking an ongoing program aimed at identifying and correcting deficiencies in the treatment of confidential information by listed companies. This work aligns with our strategic priority of promoting fair and efficient markets.
- 38 In REP 405, we discussed the release of Report 393 *Handling of confidential information: Briefings and unannounced corporate transactions* (REP 393) in May 2014. This work continued into the most recent period, as we considered the possible occurrence of selective analyst briefings by entities before market-sensitive announcements and related share price movements in their securities. The purpose of these studies is to identify potential entities, brokers and analysts who may have been involved in possible market misconduct.
- 39 We aim to achieve positive behavioural change in the market through more appropriate disclosure of confidential information. Where we identify inappropriate disclosures, we may take enforcement action.

Example 4: Handling of confidential information

We are currently reviewing analysts' re-ratings for the last four years and comparing them to the timing of publicly-available information. This review may identify potential leakages of confidential information that we will need to further investigate.

Designated trading representatives**Orders rejected by system filters**

- 40 The majority of trading orders in Australian are electronically transmitted to financial markets. Designated trading representatives (DTRs) are generally the final point of entry for orders rejected by system filters. As such, DTRs play a vital role in maintaining market integrity.
- 41 Our Market Surveillance team continues to encounter issues with automated trade filters and trading anomalies associated with DTR execution of orders which have been rejected by system filters. We have observed instances where DTRs are entering these orders without first considering the subsequent market impact.
- 42 Market participants must ensure they have appropriate system controls and filters in place for trades they execute electronically. In particular, participants should ensure DTRs give due regard to the consequences of their actions at all times. We will continue to monitor the market for occurrences of this conduct.

Crossing system reviews

- 43 ASIC has begun a thematic review of crossing systems and will be testing how crossing system operators are meeting their regulatory obligations—particularly the market integrity rules that were implemented since the dark liquidity taskforce (e.g. public and private disclosure requirements).

Client money

- 44 Through our MSUs and other publications, we have consistently communicated to industry that the protection of client money is high of priority. We have increased focus on this area due to ongoing concerns, and will conduct a series of targeted compliance reviews within the next 12 months.

The role of gatekeepers

- 45 Gatekeepers perform an important role in encouraging sound investment practices, detecting and preventing market failures and promoting market integrity. This role is vital to ensuring a fair and efficient financial system.

- 46 Market licensees and market participants act as gatekeepers for Australian financial markets. Functions they perform as gatekeepers include:
- (a) verifying, certifying, approving and recommending products and services to investors;
 - (b) monitoring compliance by entities and their management;
 - (c) undertaking private supervision through the detection and deterrence of misconduct; and
 - (d) ensuring markets are fair, orderly and transparent.
- 47 We expect these gatekeepers to adhere to the highest standards in performing their duties. We will hold them to account for any failure to meet and maintain these standards through enforcement action.

A Market surveillance

Key points

This section provides details of our real-time market surveillance activity and markets enquiries for the relevant period.

Real-time surveillance of Australia's licensed financial markets

- 48 Sophisticated surveillance technologies, together with staff experienced in trading and trading technology, are assisting us to more effectively detect, understand and respond to changing market conditions, patterns and trends.

Market analysis and intelligence

- 49 Our supervision of financial markets continues to be enhanced by the successful rollout of our new market surveillance system, MAI. Purpose-built and designed to handle the dynamic nature of Australia's financial markets, MAI allows for the examination of very large data sets and the review of granular information on the behaviour of high-frequency trading and algorithmic traders.
- 50 MAI system developments are ongoing and, during the relevant period, enabled ASIC surveillance analysts to more fully examine historical trading data and more quickly identify anomalous trading activity which may require investigation. As noted previously, the flexibility of the system has allowed ASIC to implement a Rapid Application Development process, enabling the design, testing, implementation and release of additional MAI alerts and reports on an 'as-needs' basis: see REP 405.

Trade surveillance reports

- 51 Trade surveillance alerts are indicators of unusual trading activity. During the relevant period, there were 19,375 alerts compared to 17,091 alerts in the previous period: see Table 2.
- 52 The overall number of alerts generated in any one period is usually affected by a number of factors, including the level of corporate transactions, general market volatility and trading conditions. During the relevant period, the slight increase in alerts was consistent with the overall increase in trading volumes for the period. We nevertheless expect that future MAI enhancements will continue to contribute to even greater refinement and calibration of alerts and reports, and result in further efficiencies.

- 53 An important development for ensuring ongoing MAI efficiencies was the implementation of enhanced regulatory data. From 28 July 2014, participants have been required to provide specified data on orders to market operators, who must record and provide to ASIC all regulatory data they receive. This development provides ASIC with far greater visibility of individual traders and trading behaviour and, importantly, immediacy of information (now available in real-time). Previously, we only had access to this information for a small percentage of traders in real time.
- 54 Enhanced regulatory data has increased ASIC's capability to monitor markets, while at the same time decreasing the amount of work associated with issuing and responding to statutory notices for information in similar cases. ASIC's Surveillance team can now examine individual and account activity over an extended period, to more efficiently identify suspicious transactions which may warrant further investigation.

Table 2: Trade surveillance alerts

Surveillance activity	Previous periods		Relevant period
	1 July–31 Dec 2013	1 Jan–30 June 2014	1 July–31 Dec 2014
Total number of alerts	19,255	17,091	19,375

Derivatives surveillance

- 55 The continued operation of a dedicated Derivatives Surveillance team, established in November 2013, together with ongoing MAI system enhancements, has changed the way we undertake derivatives surveillance. MAI has largely automated processes that were previously manual and time-intensive. We can now examine extended trading periods in greater depth, for example, by looking at individual participant accounts.

Market enquiries

- 56 When our surveillance analysts cannot explain an alert or series of alerts by reference to available market information (e.g. through the media, internet chat sites, broker research and dialogue with brokers), we may conduct market enquiries. However, not all enquiries are the result of MAI alerts. Enquiries are also generated by surveillance analysts in response to market participant breach reports, referrals from other ASIC teams and reports of misconduct by individuals and entities: see paragraphs 85–91.
- 57 We may call on market participants, companies, advisers and investors to assist us with the conduct of enquiries. We may also use our compulsory

information gathering powers to obtain information from participants, clients, listed entities, and corporate and other advisers, where necessary.

- 58 The number of enquiries undertaken in the relevant period fell marginally: see Table 3. There were 112 enquiries undertaken during the relevant period, compared with 122 and 102 in the preceding two periods. More than half of these enquiries related to insider trading and are largely attributable to rising corporate activity in the Australian market, including takeovers, capital raisings and earning upgrades/downgrades. Increased activity by the Derivatives Surveillance team also contributed to the overall increase in insider trading enquiry numbers.
- 59 Continuous disclosure enquiries are generated by ASIC surveillance analysts as well as referrals from ASX: see paragraph 85. The number of continuous disclosure-related enquiries fell. There was also a slight fall in the number of enquiries relating to breaches of market integrity rules.

Table 3: Markets enquiries

Alleged offence	Previous periods		Relevant period
	1 July–31 Dec 2013	1 Jan–30 June 2014	1 July–31 Dec 2014
Insider trading	53	51	55
Market manipulation	21	32	27
Continuous disclosure	13	14	8
Breach of market integrity rules	15	25	22
Total	102	122	112

- 60 In the relevant period, ASIC's Market and Participant Supervision (MPS) team referred a total of 36 matters to the Market Integrity Enforcement team for investigation, an increase from 21 for the previous period. This included 20 referrals for conduct involving suspected insider trading and five referrals for conduct involving suspected market manipulation.

Other surveillance activities

- 61 Automated trading and subsequent DTR action continues to be a key area of focus for our surveillance activities. The use of anomalous order controls and market participant filters has greatly reduced the incidence of trade cancellations and disorderly markets in equity market products. However, there has been an increasing trend of trade cancellations and disorderly markets in exchange traded options and warrants.

- 62 Where we have raised this issue directly with market participants, they have responded by agreeing to put in place new filters and processes to ensure that these orders are more effectively managed by their automated order processing (AOP) systems or are reviewed by an appropriately-skilled DTR before being released to the market. However, we have observed that some DTRs have not always adequately considered the effect of releasing system-rejected orders into the market.
- 63 Market participants are responsible for ensuring that their technology systems are appropriate. This includes technology provided by key vendors. Market participants cannot outsource their responsibilities and obligations in this area and need to ensure due diligence is performed with any system changes or implementations. Table 4 summarises instances where discussions with participants have led to the amendment of order execution methods and review of trading algorithms or filters.

Table 4: Other surveillance activities

Other surveillance activities	Previous periods		Relevant period
	1 July–31 Dec 2013	1 Jan–30 June 2014	1 July–31 Dec 2014
Execution strategy	11	17	14
Algorithmic trading and filter issues	7	9	6
Other	8	4	6
Total	26	30	26

Reporting markets or trading issues

- 64 Market participants who wish to discuss markets and trading matters with ASIC, including:
- (a) concerns or queries relating to trading anomalies;
 - (b) unexplained market events;
 - (c) suspicious market trades or behaviour; or
 - (d) concerns about misconduct in the market.

should contact MPS via the hotline or email address below:

Hotline: 1300 029 454

Email: markets@asic.gov.au.

B Supervision of market participants and securities dealers

Key points

This section describes our supervision of market participants and securities dealers during the relevant period.

Compliance activity

Risk-based assessments

- 65 Risk-based assessments of all market participants are conducted by ASIC on a rolling basis. In the relevant period, we commenced 14 risk-based assessments of participants and completed six—down from 35 in the previous period. This decrease is due to seasonal work such as renewing the accreditations of ADAs, reviewing AOP notifications and training new resources to complete the risk-based assessments. We also allocated significant resources to other projects, such as MECS.
- 66 Engagement with industry through presentations and liaison meetings helps develop our relationships with market participants and provides information on topical issues and potential risks facing the industry. During the relevant period, we undertook 99 industry presentations on markets-related issues: see Table 5. The increase was primarily due to greater engagement with industry during the introduction of MECS and a new method of reporting industry presentations.

Compliance reviews

- 67 Market participants are required to have arrangements in place to monitor compliance with the Corporations Act and market integrity rules. During the relevant period, we completed 45 participant compliance reviews—this was a slight decrease from the previous period (55 compliance reviews completed).
- 68 In our compliance reviews, we continue to note some shortcomings in the monitoring and supervision of advisers and DTRs due to non-compliance with procedures, insufficient resources and a lack of oversight in regional or branch offices.
- 69 We continue to work with a number of market participants to ensure that there are sufficient compliance resources to monitor and supervise their businesses—taking into consideration factors such as the nature, size and complexity of their business.

70 During our compliance reviews we identified serious concerns in relation to the compliance resources, monitoring and risk management frameworks of some market participants and securities dealers—in particular, inadequate arrangements to monitor staff trading and the management of conflicts of interest. We intend to conduct a specific review of the management of confidential information over the next 6–12 months.

71 We have also spent more time dealing with matters concerning client money, and will focus more attention on this area as part of a dedicated compliance review in the next 6–12 months.

General or personal advice

72 We are concerned about the high proportion of general advice compared to personal advice, particularly by full-service brokers. We intend to focus more efforts on reviewing the provision of advice by market participants, whether it is being categorised correctly as personal or general advice, and whether the relevant obligations are complied with appropriately. This may include a focus on management oversight and adviser training.

73 To date, our compliance reviews have identified deficiencies with the provision of personal advice and the requirement to provide a clear, concise and effective Statement of Advice. For example, we identified market participants that had not provided sufficient information to clients regarding the basis on which the advice was given—suggesting that inadequate consideration may have been given to clients’ circumstances, goals and objectives.

Discretionary trading

74 We continued to focus on instances of unauthorised discretionary trading. For market participants with licence authorisations to conduct managed discretionary trading, we reviewed their processes to ensure compliance with the relevant requirements. In some instances, additional guidance was provided to ensure that participants’ obligations were met.

Suspicious activity reporting

75 In REP 405, we noted that we would focus on participants’ compliance with the suspicious activity reporting (SAR) obligations, including inspection of breach and incident registers. We will continue this review over the next six months.

76 Some participants only refer matters to the Australian Transaction Reports and Analysis Centre (AUSTRAC) or conduct their own investigations—and only when that investigation is complete will they consider reporting the matter to ASIC or AUSTRAC. Our previous reviews of trade monitoring revealed that some participants retained only limited documentary evidence of monitoring activity, did not have detailed policies and procedures in place, and had limited involvement by a responsible executive.

- 77 The importance of SAR is reflected in the number of reported matters being referred to ASIC's Enforcement team for further investigation. For example, over 20% of SARs (up to 31 December 2014) were referred to Enforcement.

Facilitation

- 78 During the relevant period, we conducted a review of principal trading and facilitation to better understand the nature, extent and conduct of these activities—and the controls and supervision arrangements in place to manage potential conflicts of interest. We intend to provide feedback to the market participants that participated in the review, and provide information to the broader market on this issue, in due course.
- 79 We are concerned that active facilitation poses increased risks for the management of conflicts of interest, confidentiality of client order information and best interests of the client. Also of concern are staff that hold dual roles and have, or may obtain, access to client order flow information that presents a conflict of interest.

Further compliance reviews

- 80 Additional reviews undertaken during the period that will be discussed further in the next report include our compliance reviews of outsourcing, crossing systems, hybrids and post-trade filters.
- 81 To date, our review of outsourcing arrangements has identified an absence of disaster recovery plans and deficiencies in service level agreements held between market participants and their outsourced provider.
- 82 During our post-trade filter reviews, we have had to remind participants of their record-keeping obligations during investigations into filter breaches (including providing evidence of responsible executive oversight).
- 83 Table 5 provides a summary of key market participant supervision activity. This table summarises the risk assessments and compliance reviews, including thematic reviews, proactive and reactive surveillances. Following a review we may provide observations and recommendations to the participant that may require remediation: see paragraph 18. We then monitor and review the follow-up action that has been undertaken by the participant.

Table 5: Participant risk assessments and compliance reviews

Activity	Previous periods						Relevant period			
	1 July–31 Dec 2013			1 Jan–30 June 2014			1 July–31 Dec 2014			
	Outstanding (30 June 2013)	New	Completed	Outstanding (31 Dec 2013)	New	Completed	Outstanding (30 June 2014)	New	Completed	Outstanding (31 Dec 2014)
Compliance reviews (includes business-as-usual equities and futures participants, reactive, proactive and targeted)	59	66	73	52	31	55	28	48	45	31
Monitoring and remediation	7	3	6	4	2	4	2	2	1	3
Risk-based assessment visits	9	18	17	10	25	35	–	14	6	8
Other (e.g. industry presentations)	–	22	22	–	17	17	–	99	99	–

84 Applications and notifications to ASIC in the relevant period included the renewal of ADAs and the updating of management structures. In accordance with the market integrity rules, market participants must submit details of their management structures when there has been a material change.

Table 6: Applications, waivers, notifications and exemptions

Applications, waivers, notifications and exemptions	Previous periods						Relevant period			
	1 July–31 Dec 2013			1 Jan–30 June 2014			1 July–31 Dec 2014			
	Outstanding (1 July 2013)	New	Completed	Outstanding (31 Dec 2013)	New	Completed	Outstanding (30 June 2014)	New	Completed	Outstanding (31 Dec 2014)
Applications	3	84	83	4	90	93	1	264	261	4
Waivers requested (ASX)	–	7	7	–	2	2	–	10	9	1
Waivers requested (ASX 24)	1	4	3	2	–	2	–	4	3	1
Waivers requested (Chi-X)	–	6	6	–	1	1	–	6	5	1
Waivers requested (NSX)	1	–	1	–	–	–	–	–	–	–
Waivers requested (Competition)	–	5	5	–	2	2	–	2	2	–
Waivers requested (APX)	–	–	–	–	3	1	2	1	3	–
Relief applications	4	11	14	1	3	4	–	7	5	2
AOP certifications received (includes significant changes)	2	23	23	2	11	13	–	62	60	2
Notifications (includes professional indemnity insurance, responsible executive changes and ADA withdrawals)	7	314	302	19	151	154	16	358	351	23

Note: 'Completed' includes applications, waivers and relief applications where an in-principle decision has been made, but is yet to be finalised. This is consistent with the ASIC Service Charter.

Referrals about market participants

- 85 The following referrals about market participants were received by ASIC in the relevant period:
- (a) four breaches of the Corporations Act or market integrity rules (or both) were reported by auditors of market participants relating to the actions of those market participants;
 - (b) two complaints about market participants and securities dealers were received from members of the public;
 - (c) 12 referrals (five relating to the same entity) were received from ASX in relation to continuous disclosure activities; and
 - (d) two referrals were received from ASX in relation to participant misconduct issues such as AOP and filter or trust account issues.
- 86 Complaints about the conduct of market participants may be directed to the MPS team using the hotline or email address below:
- Hotline: 1300 029 454
- Email: market.participants@asic.gov.au

Self-reporting to ASIC

- 87 Market participants that breach their AFS licence are required to self-report to ASIC. Participants that fail to do so can expect greater scrutiny and possible enforcement action from ASIC. We expect to see stronger action from industry in this area in the future.
- 88 It is the responsibility of market participants to report compliance issues to ASIC. We expect participants to come to ASIC with problems they have identified, as part of the process of fixing those problems.
- Note: The benefits of cooperating with ASIC, and the factors we take into account when assessing cooperation, are explained in Information Sheet 172 *Cooperating with ASIC* (INFO 172).
- 89 In the relevant period, we received 22 breach notifications from market participants, of these:
- (a) four breaches of the Corporations Act were self-reported by market participants;
 - (b) 16 breaches of market integrity rules were self-reported by market participants; and
 - (c) two breaches of both the Corporations Act and market integrity rules were self-reported by market participants.

90 In addition, 21 trust account notifications were made under market integrity rules by market participants.

91 Market participants should report significant breaches under s912D of Corporations Act using the dedicated email address below:

Email: fsr.breach.reporting@asic.gov.au

Engagement with ASIC

92 ASIC continues to engage in an ongoing dialogue with market participants. We use this dialogue to improve processes and procedures to address less serious issues identified by our market surveillance analysts. Importantly, this dialogue does not replace enforcement action, which we will pursue for serious breaches of the law and market integrity rules.

93 We encourage market participants to raise any trading issues or concerns with us at an early stage. The MPS team may be contacted through the hotline or using the email address below:

Hotline: 1300 029 454

Email: market.participants@asic.gov.au

C Market enforcement outcomes

Key points

This section provides a summary of ASIC's market enforcement outcomes for the relevant period, as well as a comparison of two-year periods since 2011. Given the time taken to identify and investigate cases, we consider a two-year reporting period provides a clearer indication of trends in enforcement outcomes.

Investigation and enforcement outcomes

- 94 Enforcement action is about punishing wrongdoing and ensuring that the threat of punishment (and the impact the threat has on individuals and companies) positively shapes their behaviour and compliance. Enforcement is a process that takes significant time and resources—and the outcome is often contingent on the availability of evidence. For this reason, we seek to maximise the deterrence value of our enforcement activities.
- 95 Table 7 outlines significant market enforcement outcomes for the two-year period from 1 January 2013 to 31 December 2014, compared to the preceding two-year period ending 31 December 2012. It includes a 'snapshot' of the outcomes for the six-month period ending on 31 December 2014.

Table 7: Investigation and enforcement outcomes

Significant market integrity-related outcomes	Previous two-year period	Current two-year period	
	1 January 2011– 31 December 2012 (two years)	1 January 2013– 31 December 2014 (two years)	1 July 2014– 31 December 2014 (six months)
Bannings	–	1	–
Insider trading pleas, verdicts and judgments	9	18	3
Continuous disclosure infringement notices	6	6	–
Other sanctions (enforceable undertakings and pecuniary penalties)	13	8	4
Market manipulation pleas, verdicts and judgments	1	4	2
Infringement notices issued by the MDP	11	24	8
Total	40	61	17

Examples of ASIC enforcement outcomes

Insider trading

- 96 Insider trading is a form of theft and will not be tolerated. We are committed to prosecuting insider trading. Our ability to monitor trading as it occurs, watch for trading in stocks we know are in play and invoke our investigatory powers early, means that we are a credible insider trading enforcement agency.
- 97 Using MAI, it is easier than ever before for ASIC to identify suspicious trading by connecting patterns and relationships. This is essential for greater levels of detection of insider trading relationships and market manipulation.
- 98 In the relevant period, we achieved three enforcement outcomes against individuals for insider trading activity: see Example 5.

Example 5: Communicating information about a takeover

Two Sydney men plead guilty to insider trading charges which netted a profit of more than \$180,000.

An ASIC investigation determined that Daniel Joffe, an Associate Analyst with Moody's, had shared information with Nathan Stromer, who then bought and sold shares and CFDs in companies that were about to be, or likely to be subject to, takeover bids and price-sensitive announcements.

The pair admitted that:

- between 10 and 14 November 2006, Mr Joffe received inside information relating to a proposed takeover of Alinta Infrastructure Holdings Limited (AIH) by Alinta Limited and passed this information to Mr Stromer who acquired 962,000 CFDs in AIH; and
- between 1 and 8 August 2006, Mr Joffe became aware of inside information relating to a proposed takeover of Auckland International Airport Limited (AIA) by Babcock & Brown Limited. Mr Joffe communicated this information to Mr Stromer and procured him to acquire 29,580 AIA shares.

Mr Joffe has admitted that between 20 and 27 September 2006, he communicated inside information relating to upcoming price-sensitive announcements contemplated by the Australian Wheat Board Limited (AWB) to Mr Stromer and procured him to short sell 135,000 AWB CFDs.

The matter will return to the Supreme Court of NSW for sentencing hearing on 27 April 2015.

- 99 Directors and company officers should exercise caution when trading in the shares of their company or its related entities. This is not only to ensure that they comply with insider trading laws, but also to avoid any perception that they may have benefited from their position.

- 100 We expect company boards and investors to fulfil their duty to ensure compliance with insider trading laws and to consider the acceptability of conduct that does not breach the law, but which may nonetheless impact on investor confidence.
- 101 ASIC's role is to thoroughly investigate potential insider trading breaches and, where sufficient evidence exists, take enforcement action to uphold insider trading laws. We also facilitate discussions with industry and companies about legal requirements and best practice. For example, earlier this year, we hosted a roundtable meeting to discuss specific governance issues, including director trading.

Market manipulation

- 102 It is an offence under the Corporations Act to create a false or misleading appearance of:
- (a) active trading in financial products on a financial market;
 - (b) the market for financial products on a financial market; or
 - (c) the trading price for financial products on a financial market.

This type of behaviour is a form of market manipulation.

- 103 Market manipulation damages market and investor confidence, leading to inefficient markets and uninformed consumers. Where we identify market manipulation we will take enforcement action. In the relevant period, we achieved one outcome relating to market manipulation: see Example 6.

Example 6: NSW man charged with market manipulation

Former GTG Chief Executive, Dr Mervyn Jacobson, was convicted of manipulating the share price of GTG on the ASX market.

He was sentenced on 28 November 2014, to a total term of two years and eight months, with his conviction and sentence following an eight-week jury trial in the Supreme Court of Victoria. Evidence was heard of Dr Jacobson's actions to manipulate the GTG share price on ASX to help him minimise and manage margin calls on loans totalling approximately \$12 million.

In sentencing Dr Jacobson, Justice Stephen Kaye said the offences for which he had been convicted were serious, and that his conduct 'had the capacity to erode the integrity of, and public confidence in, the securities market, and thereby to cause damage to members of the community, who have invested their savings in that market.'

ASIC's investigation into this matter followed a referral from ASX. The Commonwealth Director of Public Prosecutions prosecuted this matter.

All of Dr Jacobson's co-conspirators have previously been convicted and received sentences of imprisonment for their role in the conduct, following ASIC's investigations.

Continuous disclosure breaches

- 104 Continuous disclosure by listed companies is fundamental to market integrity and transparency. Failure to abide by continuous disclosure obligations can cause serious damage to individual investors, as well as the integrity and transparency of our financial markets.
- 105 Broadly speaking, we consider compliance with the continuous disclosure obligations in Australia is generally good. We take very few actions relative to the number of announcements made, and far fewer than market commentators say ‘must’ be breaches.
- 106 We will continue to use our enforcement powers to highlight the importance of this obligation. Continuous disclosure infringement notices are designed to provide a fast and effective remedy for less serious breaches, so that redress is proportionate and proximate in time to the breach. We consider infringement notices to be a very important and useful tool in ASIC’s regulatory toolkit.
- 107 In the relevant period, two infringement notices were issued to companies for continuous disclosure breaches: see Example 7. In addition, the highest civil penalty ever imposed in Australia for a continuous disclosure breach was made against Newcrest Mining Limited (Newcrest), following an ASIC investigation.

Example 7: Newcrest pays \$1.2 million for breach of continuous disclosure obligations

On 2 July 2014, the Federal Court imposed a \$1.2 million penalty on Newcrest for contravention of its continuous disclosure obligations.

ASIC issued proceedings against Newcrest on 18 June 2014, alleging that in a series of briefings to analysts, Newcrest disclosed:

- from 28 May 2013, information regarding Newcrest’s expected gold production for the 2013–14 financial year; and
- on 5 June 2013, information regarding Newcrest’s expected capital expenditure for the 2013–14 financial year.

Newcrest admitted the contraventions and the parties filed a joint application for civil penalties to be imposed. The court found that Newcrest contravened its continuous disclosure obligations under s674(2) of the Corporations Act.

In handing down his judgment, the Hon Justice Middleton said that ‘the penalties are such to send a strong message to market participants to be mindful of the care and caution needed when interacting with analysts... [and]...also reinforce the message that equal access to market sensitive information is paramount in ensuring that markets operate on an informed, and equally informed, basis.’

Enforceable undertakings

- 108 ASIC pursues negotiated outcomes (which may arise from surveillances or investigations), including enforceable undertakings. Negotiated outcomes,

such as enforceable undertakings, can offer a faster, more flexible and effective regulatory outcome than might otherwise be achieved through administrative or civil action. Compared with court proceedings, enforceable undertakings also provide greater scope to influence future conduct.

- 109 We will enter into an enforceable undertaking only if we consider it provides a more effective regulatory outcome than non-negotiated, administrative or civil sanctions. Enforceable undertakings may require the subject to pay compensation to consumers, improve internal compliance arrangements or appoint an independent expert to oversee elements of the entity's business and report back to ASIC on performance: see Example 8.

Example 8: Enforceable undertaking for potential misconduct involving a bank bill swap rate

On 21 July 2014, ASIC accepted an enforceable undertaking from the Royal Bank of Scotland N.V. (RBS) in relation to potential misconduct involving a bank bill swap rate. RBS will also make a voluntary contribution of \$1.6 million to fund independent financial literacy projects in Australia.

The enforceable undertaking requires RBS to ensure its contribution to Australian interest rate benchmark settings is compliant with its obligations under orders made by the US Commodity Futures Trading Commission. RBS is also required to undertake certain remedial measures for trading in reference bank bills. An independent compliance expert will be required to review and report on RBS's compliance with the enforceable undertaking in respect of these remedial measures. ASIC will make public the outcome of that review.

Note: Our policy regarding enforceable undertakings is contained in Regulatory Guide 100 *Enforceable undertakings* (RG 100). Copies of enforceable undertakings are available on [our website](#).

Markets Disciplinary Panel

- 110 The MDP is an independent peer-review body that exercises ASIC's power to issue infringement notices and accept enforceable undertakings in relation to alleged breaches of market integrity rules.
- 111 In the relevant period, the MDP issued seven infringement notices for contraventions of market integrity rules, all of which were complied with. These were:
- (a) Goldman Sachs Australia Pty Ltd paid a penalty of \$35,000 to comply with an infringement notice given to it by the MDP. The penalty was for failing to prevent the entry into the ASX trading platform of an erroneous order which resulted in the market for AP Eagers Limited ordinary shares not being both fair and orderly: see Media Release [\(14-216MR\)](#) *Goldman Sachs Australia Pty Ltd pays \$35,000 infringement notice penalty* (1 September 2014).

- (b) Taylor Collison Limited paid a penalty of \$30,000 to comply with an infringement notice given to it by the MDP. The penalty was for failing to prevent the entry into the ASX trading platform of an erroneous order which resulted in the market for BC Iron Limited ordinary shares not being both fair and orderly: see Media Release ([14-217MR](#)) *Taylor Collison Limited pays \$30,000 infringement notice penalty* (1 September 2014).
- (c) Merrill Lynch Equities (Australia) Limited paid a total penalty of \$96,000 to comply with an infringement notice given to it by the MDP: see Media Release ([14-228MR](#)) *Merrill Lynch Equities (Australia) Limited pays \$96,000 infringement notice penalty* (11 September 2014). The penalty was for failing to:
 - (i) have in place an appropriate automated price filter in relation to AOP for one client account, which interfered with the efficiency and integrity of the ASX market; and
 - (ii) prevent entry into the ASX trading platform of an erroneous order which resulted in the market for Class A non-voting common stock in News Corporation Inc. not being both fair and orderly.
- (d) BBY Limited paid a penalty of \$90,000 to comply with an infringement notice given to it by the MDP. The penalty was for failing to ensure that its AOP system had in place organisational and technical resources, including having appropriate automated filters for 30 client accounts—and processes to record any changes to the automated filters without interfering with the efficiency and integrity of the ASX market or the proper functioning of the ASX trading platform: see Media Release ([14-229MR](#)) *BBY Limited pays \$90,000 infringement notice penalty* (11 September 2014).
- (e) Etrade Australia Securities Limited paid a penalty of \$55,000 to comply with an infringement notice given to it by the MDP. The penalty was for failing to prevent the entry into the ASX trading platform of an erroneous order which resulted in the market for SPDR MSCI Australia Select High Dividend Yield Fund units not being both fair and orderly: see Media Release ([14-246MR](#)) *Etrade Australia Securities Limited pays \$55,000 infringement notice penalty* (23 September 2014).
- (f) Commonwealth Securities Limited paid a penalty of \$15,000 to comply with an infringement notice given to it by the MDP. The penalty was for failing to prepare and provide accurate crossing system monthly reports to ASIC: see Media Release ([14-280MR](#)) *Commonwealth Securities Limited pays \$15,000 infringement notice penalty* (27 October 2014).
- (g) ABN AMRO Clearing Sydney Pty Ltd paid a penalty of \$40,000 to comply with an infringement notice given to it by the MDP. The penalty was for failing to demonstrate prudent risk management procedures by not setting and documenting appropriate maximum price change limits as required: see Media Release ([14-281MR](#)) *ABN AMRO Clearing Sydney Pty Ltd pays \$40,000 infringement notice penalty* (27 October 2014).

112 Pursuant to regs 7.2A.15(4)(b)(i)–(ii) of the Corporations Regulations 2001, each of the parties named above have complied with the respective infringement notice. Compliance is not an admission of guilt or liability, and none of the parties are taken to have contravened s798H(1) of the Corporations Act.

Note 1: Infringement notices for these and other matters are available on [our website](#).

Note 2: Our policy regarding the MDP is contained in Regulatory Guide 216 *Markets Disciplinary Panel* (RG 216) and Regulatory Guide 225 *Markets Disciplinary Panel practices and procedures* (RG 225).

Appendix: Schedule of media releases

Table 8: Media releases

Media release	Release date
14-148MR Newcrest ordered to pay \$1.2 million for breaching continuous disclosure laws	2 July 2014
14-156MR Former portfolio manager sentenced to jail	4 July 2014
14-169MR ASIC accepts enforceable undertaking from The Royal Bank of Scotland	21 July 2014
14-179MR Jonathan Moylan convicted	25 July 2014
14-186MR Former director of Northern Star Resources Limited charged with insider trading	1 August 2014
14-216MR Goldman Sachs Australia Pty Ltd pays \$35,000 infringement notice penalty	1 September 2014
14-217MR Taylor Collison Limited pays \$30,000 infringement notice penalty	1 September 2014
14-228MR Merrill Lynch Equities (Australia) Limited pays \$96,000 infringement notice penalty	11 September 2014
14-229MR BBY Limited pays \$90,000 infringement notice penalty	11 September 2014
14-246MR Etrade Australia Securities Limited pays \$55,000 infringement notice penalty	23 September 2014
14-270MR New South Wales man pleads guilty to market manipulation	14 October 2014
14-280MR Commonwealth Securities Limited pays \$15,000 infringement notice penalty	27 October 2014
14-281MR ABN AMRO Clearing Sydney Pty Ltd pays \$40,000 infringement notice penalty	27 October 2014
14-320MR Former Genetic Technologies CEO jailed for market manipulation	28 November 2014
14-326MR Two Sydney men plead guilty to insider trading	5 December 2014
14-339MR Avestra Asset Management fined for breaching takeover laws	17 December 2014
14-345MR ASIC accepts enforceable undertaking from First Prudential Markets on compliance processes	19 December 2014

Key terms

Term	Meaning in this document
ADA	Accredited derivatives adviser
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries out a financial services business to provide financial services Note: This is a definition contained in s761A of the Corporations Act.
AFS licensee	A person who holds an AFS licence under s913B of the Corporations Act Note: This is a definition contained in s761A of the Corporations Act.
algorithm or algorithmic trading	Electronic trading activity where specific execution outcomes are delivered by predetermined parameters, rules and conditions
AOP (automated order processing)	The process by which orders are registered in a market participant's system, which connects it to a market. Client or principal orders are submitted to an order book without being manually keyed in by an individual (referred to in the rules as a designated trade representative or 'DTR'). It is through AOP systems that algorithmic programs access our markets
APX	Asia Pacific Exchange Limited or the exchange market operated by APX Limited
ASIC	Australian Securities and Investments Commission
ASIC Market Integrity Rules (ASX Market) 2010	Rules made by ASIC under s798G of the Corporations Act for trading on ASX
ASX	ASX Limited (ACN 008 624 691) or the exchange market operated by ASX Limited
ASX 24	The exchange market formerly known as Sydney Futures Exchange, operated by Australian Securities Exchange Limited
Australian market licence	An Australian market licence under s795B of the Corporations Act that authorises a person to operate a financial market
CFD	Contract for difference
Chi-X	Chi-X Australia Pty Ltd (ACN 129 584 667) or the exchange market operated by Chi-X
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act

Term	Meaning in this document
DTR (designated trading representative)	A representative of the market participant that has been authorised by the participant to submit trading messages to the trading platform on behalf of the participant
enforceable undertaking	An enforceable undertaking that may be accepted by ASIC under reg 7.2A.01 of the Corporations Regulations 2001
equity market products	Shares, managed investment schemes, the right to acquire by way of issue shares and managed investment schemes, and CHESS Depository Interests admitted to quotation on ASX
financial market	As defined in s767A of the Corporations Act. It encompasses facilities through which offers to acquire or dispose of financial products are regularly made or accepted
high-frequency trading	While there is not a commonly agreed definition of high-frequency trading, we characterise it as: <ul style="list-style-type: none"> • the use of high-speed computer programs to generate, transmit and execute orders; • the generation of large numbers of orders, many of which are cancelled rapidly; and • the holding of positions for very short time periods, typically ending the day with a zero position
infringement notice	An infringement notice issued under reg 7.2A.04 of the Corporations Regulations 2001
market integrity rules	Rules made by ASIC, under s798G of the Corporations Act, for trading on domestic licensed markets
market licensee	Holder of an Australian market licence
market manipulation	As defined in Pt 7.10 of the Corporations Act
market participant	An entity that is a participant of a financial market on which equity market products are quoted
MAI	ASIC's Market Analysis and Intelligence surveillance system
MDP (Markets Disciplinary Panel)	ASIC's Markets Disciplinary Panel, through which ASIC exercises its power to issue infringement notices and to accept enforceable undertakings in relation to breaches of the market integrity rules
MECS	ASIC's Market Entity Compliance System
MPS	ASIC's Market and Participant Supervision team
NSX	National Stock Exchange of Australia Limited (ACN 000 902 063) or the exchange market operated by NSX Limited (formerly known as the Newcastle Stock Exchange).
securities dealer	An AFS licensee who is not a market participant but sells securities products through a market participant

Term	Meaning in this document
Statement of Advice	<p>A document that must be given to a retail client for the provision of personal advice under Subdivs C and D of Div 3 of Pt 7.7 of the Corporations Act</p> <p>Note: See s761A of the Corporations Act for the exact definition.</p>
surveillance	<p>The process of gathering and analysing particular information on a particular market participant or other relevant entity. ASIC conducts surveillance to assess and enforce compliance with financial services laws and ASIC market integrity rules to produce constructive change by all market participants and to promote public confidence in Australia's financial markets and its participants</p>