DISCIPLINARY MATTER – D2MX Pty Ltd

D2MX Pty Ltd ("D2MX") has paid a penalty of <u>**$120,000**</u> to comply with an infringement notice given to it by the Markets Disciplinary Panel ("MDP").

The penalty was for D2MX:

- failing to have in place organisational and technical resources, including having:
    - 'price movement' automated filters as appropriate, for 95 DMA client accounts between August 2011 to 21 March 2014; and

    - processes to verify that the 'price movement' automated filters were successfully applied to the 95 DMA clients,

    which interfered with the efficiency and integrity of the Market; and

- Failing to prevent the entry into the ASX Trading Platform of an erroneous Order which resulted in a market for the price of BHP CitiFirst GSL Mini Short Warrants not being both fair and orderly.

Background and circumstances

D2MX is alleged to have contravened subsection 798H(1) of the *Corporations Act 2001* ("Corporations Act") by reason of contravening Rules 5.6.3(a) and 5.9.1 of the ASIC Market Integrity Rules (ASX Market) 2010 ("MIR 5.6.3(a)" and "MIR 5.9.1").

At the relevant time, MIR 5.6.3(a) provided that:

> "*A Trading Participant which uses its system for Automated Order Processing must ensure that the system has in place:*
>
> *(a) organisational and technical resources, including having appropriate automated filters, filter parameters and processes to record any changes to the filters or filter parameters, to enable Trading Messages to be submitted into the Trading Platform without interfering with the efficiency and integrity of the Market or the proper functioning of the Trading Platform;*"

The rule has since been amended to reflect developments in Trading Participants' systems and ASIC's expectations of those systems.

MIR 5.9.1 provides:

> **"A Market Participant must not do anything which results in a market for a Product not being both fair and orderly, or fail to do anything where that failure has that effect."**

On the evidence before it, the MDP was satisfied that:

1) On 14 February 2014 at 11:14:42.04, a Direct Market Access ("DMA") client of D2MX ("Client") entered an Order into D2MX's Automated Order Processing ("AOP") system to buy 4,000 BHP CitiFirst GSL Mini Short Warrants having ASX code 'BHPLOX', at a price of $4.69 per Warrant ("Relevant Order").

2) Immediately prior to the entry of the Relevant Order by the Client into D2MX's AOP system, the market for BHPLOX was $2.68/$2.70/$3.03 (Bid/Offer/last traded price).

3) The Relevant Order traded in the market for BHPLOX as follows:

   - immediately for 2,500 BHPLOX against the priority Offer at $2.70. The Bid/Offer/last traded price following this Market Transaction was $4.69/no Offer/$2.70 with the remainder of the Relevant Order at the priority Bid of $4.69 for 1,500 Warrants; and

   - at 11:14:42.08 another Trading Participant entered an Order to sell 1,500 BHPLOX at $4.69 which traded immediately with the remaining Relevant Order ("Relevant Transaction"). Immediately following, the Bid/Offer/last traded price was $2.68/$2.70/$4.69.

4) The Relevant Transaction resulted in a $2.00 or 74% increase in the price of BHPLOX, based upon the midpoint between the Bid and Offer immediately prior to the entry of the Relevant Order.

5) The Relevant Transaction fell within the Extreme Trade Range ("ETR") under procedure 3200 of the ASX Operating Rules Procedures.

6) At about 11:16:00, the Client contacted D2MX and advised that the Relevant Order had been entered at an erroneous price.

7) At about 11:17:00, D2MX contacted the ASX and requested cancellation of the Relevant Transaction. The ASX subsequently cancelled the Relevant Transaction.

8) D2MX received no automated filter alerts or warnings after the Relevant Order was entered into D2MX's AOP system, and before the Relevant Order was submitted into the ASX Trading Platform.

9) D2MX subsequently conducted an investigation and determined that 95 DMA clients, including the Client, did not have 'price movement' automated filters applied to their Warrant market Orders from either:

   - the date of inception of the D2MX AOP system, being about August 2011; or

- the date they became clients of D2MX during the period from August 2011 to 21 March 2014.

10) During the period from August 2011 to 21 March 2014, automated filters for the 95 DMA clients were determined by D2MX and D2MX understood the filters would be applied to each client account by way of a daily upload file which was generated by a third party service provider. However, a deficiency in the daily upload file meant that the automated filters were not applied to the 95 DMA client accounts.

11) In contrast, other DMA clients of D2MX who traded Warrants through an intermediary did have 'price movement' automated filters in place from August 2011 to 21 March 2014, as the automated filters were applied manually by D2MX.

12) Between 18 February 2014 and 21 March 2014, D2MX applied the 'price movement' automated filter to Warrant market Orders placed by the 95 DMA clients.

By reason of D2MX's entry of the Relevant Order into the ASX Trading Platform on 14 February 2014, the MDP has reasonable grounds to believe that D2MX has contravened MIR 5.6.3(a) and MIR 5.9.1 and thereby contravened subsection 798H(1) of the Corporations Act.

Maximum pecuniary penalty that a Court could order

The maximum pecuniary penalty that a Court could order D2MX to pay for contravening subsection 798H(1) of the Corporations Act:

- by reason of contravening MIR 5.6.3(a), is $1,000,000;
- by reason of contravening MIR 5.9.1, is $1,000,000.

Pursuant to subsection 798K(2) of the Corporations Act, the maximum pecuniary penalty that may be imposed by the MDP and payable by D2MX under an infringement notice given for allegedly contravening subsection 798H(1) of the Corporations Act:

- by reason of contravening MIR 5.6.3(a), is $600,000;
- by reason of contravening MIR 5.9.1, is $600,000.

Penalty under the Infringement Notice

The penalties payable under the infringement notice for the alleged contraventions of subsection 798H(1) of the Corporations Act, are as follows:

- MIR 5.6.3(a) - $85,000;
- MIR 5.9.1 - $35,000.

Relevant factors

In determining this matter and the appropriate pecuniary penalty to be applied, the MDP took into account all relevant guidance and noted in particular the following:

i. the remedies applied should promote market integrity and confident and informed participation of investors in financial markets;

ii. MIR 5.6.3(a) is aimed at promoting confidence in the integrity of the market. Ensuring that Trading Participants with AOP systems have in place adequate organisational and technical resources to operate without interfering with the efficiency and integrity of the Market or the proper functioning of the Trading Platform, is critical in maintaining the integrity of the market. This includes having:

- fully functional appropriate automated filters; and

- processes to verify that appropriate automated filters are fully functional;

iii. appropriate automated filters are essential components of AOP systems used by DMA clients of Trading Participants. Appropriate automated filters are in place to ensure DMA client Orders entered through Trading Participant AOP systems are submitted into the Trading Platform without interfering with market integrity. For this reason, it is incumbent on Trading Participants (and not third parties) to ensure that their AOP systems have fully functional appropriate automated filters in place, and that their AOP systems comply with the market integrity rules. Accordingly, Trading Participants ought to exercise ongoing control over the development, implementation and maintenance of appropriate automated filters for their AOP systems instead of relying on third party service providers or vendors;

iv. D2MX failed to ensure that at all times its AOP system had in place or had activated appropriate automated filters, and failed to ensure that it had in place processes to verify that appropriate automated filters were in place or had been activated. The failure of D2MX to ensure that its AOP system had these safeguards risked undermining public confidence in the integrity of the market;

v. MIR 5.9.1 is similarly aimed at promoting confidence in the integrity of the market. Imposing a strict obligation on Market Participants not to do anything which results in a market for a Product not being both fair and orderly, is also critical in maintaining the integrity of the market;

vi. the submission of the Relevant Order into the ASX Trading Platform through D2MX's AOP system caused the price of BHPLOX to immediately increase from $2.69 to $4.69, representing a significant increase or variability of about 74%, which had the potential to impact the market;

vii. while there were two alleged breaches of the market integrity rules, being one of MIR 5.6.3(a) and one of MIR 5.9.1, both alleged breaches arose from a single course of conduct;

viii. the misconduct was of a serious nature as it had the potential to undermine confidence in the integrity of the market;

ix. the misconduct was careless on the part of D2MX. D2MX neglected to ensure that at all times its AOP system had in place or had activated, appropriate automated filters in relation to the 95 DMA client accounts;

x. the misconduct transpired over an unacceptable length of time being a period of approximately 30 months;

xi. although the misconduct did not appear to result in any benefit to D2MX or detriment to third parties, the potential to gain benefit or cause detriment was real and apparent;

xii. while the MDP had regard to D2MX self-reporting the breach of MIR 5.6.3 to ASIC, it also noted that the Relevant Transaction was initially identified by the Client, who then made D2MX aware of it;

xiii.   D2MX took immediate action on becoming aware of the Relevant Transaction in accordance with relevant ASX Operating Rules Procedures to facilitate cancellation of it;

xiv.   D2MX took steps to prevent recurrence of the breaches, including:

- immediately instigating an investigation into the cause of the resultant Relevant Transaction;
- on 18 February 2014, activating the 'price movement' automated filters for Warrant market Orders on the Client's account and three other significant DMA client accounts;
- on 21 March 2014, activating the 'price movement' automated filters for Warrant market Orders on the remaining 91 of the 95 DMA client accounts; and
- on 21 March 2014, as an additional precaution, introducing a 'general limit' automated filter.

xv.   D2MX had one prior contravention found against it by the MDP in Infringement Notice–MDP 06/14 dated 6 May 2014, relating to both MIR 5.6.3(a) and MIR 5.9.1. The MDP reiterated that any future, repeat contraventions in similar or comparable matters would not be viewed favourably;

xvi.   D2MX co-operated with ASIC throughout its investigation and did not dispute any material facts; and

xvii.   D2MX agreed not to contest the matter, thereby saving time and costs that would otherwise have been expended.

The Markets Disciplinary Panel

The MDP is a peer review body that exercises ASIC's power to issue infringement notices and accept enforceable undertakings in relation to alleged breaches of the market integrity rules. The market integrity rules are made by ASIC and apply to market operators, market participants and prescribed entities under the Corporations Regulations 2001 ("Regulations").

Additional regulatory information

Pursuant to subparagraphs 7.2A.15(4)(b)(i) and (ii) of the Regulations, D2MX has complied with the infringement notice, such compliance is not an admission of guilt or liability, and D2MX is not taken to have contravened subsection 798H(1) of the Corporations Act.

Further information on market integrity infringement notices, the market integrity rules and the MDP is available in ASIC Regulatory Guide 216–*Markets Disciplinary Panel* and ASIC Regulatory Guide 225–*Markets Disciplinary Panel practices and procedures* or at http://www.asic.gov.au under "Regulatory Resources > Markets > Market Integrity Rules" and "Regulatory Resources > Markets > Markets Disciplinary Panel".