23 September 2014 **MDP CIRCULAR 2014–13**

DISCIPLINARY MATTER – Etrade Australia Securities Limited

Etrade Australia Securities Limited ("Etrade") has paid a penalty of **<u>$55,000</u>** to comply with an infringement notice given to it by the Markets Disciplinary Panel ("MDP"). The penalty was for failing to prevent the entry into the ASX Trading Platform of an erroneous Order which resulted in a market for SPDR MSCI Australia Select High Dividend Yield Fund units not being both fair and orderly.

Background and circumstances

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

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 24 June 2013, prior to the commencement of trading on the ASX Market of the Exchange Traded Fund or ETF units in the SPDR MSCI Australia Select High Dividend Yield Fund having ASX code 'SYI':
   a) The ASX purged from the Order Book all existing Orders in SYI following an announcement made at 9:42:25 entitled "Final Distribution Announcement". The distribution was finalised as $0.17374; and
   b) The last traded price on commencement of trading was the closing price on the previous Trading Day in SYI at $27.15.
2) At 10:17:13, Etrade received from a client by Direct Market Access or DMA, an Order to sell 225 SYI at $19.92 ("Initial Order").
3) Immediately prior to the Initial Order, the market for SYI was $20.00/no ask/$27.15 (Bid/ask/last traded price).
4) On receipt, the Initial Order triggered Etrade's automated 'orderly market' filter on its Automated Order Processing or AOP system (as it was more than 5% away from the last traded price of $27.15) and was diverted to an Etrade Designated Trading Representative or DTR ("Etrade DTR 1") for assessment with the following alert or warning message 'instruction received will move the market if executed' ("Pre-trade Alert").
5) After assessing the Initial Order (by giving consideration to certain factors including the Pre-trade Alert and the market for SYI), at 10:18:13, Etrade DTR 1 submitted the Initial

Order into the ASX Trading Platform being an Order to sell 225 SYI at $19.92 ("Relevant Order").

6) The Relevant Order traded immediately in full resulting in a Market Transaction for 225 SYI at $20.00, for a total consideration of $4,500 ("Relevant Transaction").

7) The entry into the ASX Trading Platform of the Relevant Order, resulting in the Relevant Transaction, caused the price of SYI to decrease from $27.15 to $20.00, representing a $7.15 or 26% decrease in the price of SYI.

8) At 10:18:14, Etrade received the following post-trade alert ("Post-trade Alert") notifying it of the Relevant Transaction 'executed an on-market trade which moved the SYI price from $27.15 to $20.00 which represents a movement of 26% (compared to the threshold of 6.40%)'. At 10:59:21, another DTR from Etrade ("Etrade DTR 2") considered the Post-trade Alert and decided to take no action.

9) At 11:09:00, prompted by a telephone call from the ASX, a third DTR from Etrade ("Etrade DTR 3") then requested by email to the ASX that the Relevant Transaction be cancelled.

10) At 11:14:29, the ASX by its direction cancelled the resulting Market Transaction under procedure 3210 of the ASX Operating Rules Procedures at the relevant time, as it occurred within the Extreme Trade Range or ETR.

By reason of Etrade's entry of the Relevant Order into the ASX Trading Platform on 24 June 2013, the MDP had reasonable grounds to believe that Etrade contravened MIR 5.9.1 and thereby contravened subsection 798H(1) of the Corporations Act which requires compliance with the market integrity rules.

Maximum pecuniary penalty that a Court could order

The maximum pecuniary penalty that a Court could order Etrade to pay for contravening subsection 798H(1) of the Corporations Act by reason of contravening MIR 5.9.1, is $1,000,000.

Pursuant to subsection 798K(2) of the Act, the maximum pecuniary penalty that may be imposed by the MDP and payable by Etrade under an infringement notice given for contravening subsection 798H(1) of the Corporations Act by reason of allegedly contravening MIR 5.9.1, is $600,000.

Penalty under the Infringement Notice

The penalty payable under the infringement notice for the alleged contravention of subsection 798H(1) of the Corporations Act and therefore the penalty that Etrade must pay to the Commonwealth, is **$55,000.**

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:

- MIR 5.9.1 is 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 critical in maintaining the integrity of the market;
- The misconduct had the potential to damage the reputation and integrity of the market, as the submission of the Relevant Order into the ASX Trading Platform caused the price of

SYI to decrease from the last traded price of $27.15 to $20.00, representing a $7.15 or 26% decrease;

- The misconduct was negligent on the part of Etrade as the functions of Etrade DTR 1 were not exercised to the requisite high standard when Etrade DTR 1 did not take care in assessing the Initial Order, before submitting the Relevant Order into the ASX Trading Platform;
- The MDP noted in this matter that Etrade DTR 1 received and considered the Pre-trade Alert prior to the Relevant Order being submitted into the ASX Trading Platform, however this did not prevent the misconduct the subject of this matter. An important aspect of the role of the DTR, as an internal control, is to take proper care and pay proper attention and diligence in the consideration of pre-trade alerts or warnings especially in circumstances where the alert triggered is in relation to an Order received through an AOP system via DMA. Taking care and paying attention and diligence to prevent the entry of Orders into the Trading Platform that could result in a market that is not both fair and orderly, is a critical measure in maintaining the integrity of a market;
- Although not impacting cancellation of the Relevant Transaction, the MDP also noted in this matter that Etrade DTR 2 received and considered the Post-trade Alert after the Relevant Transaction but failed to take any action. Another important aspect of the role of the DTR, as an internal control, is to take proper care in addition to paying proper attention and diligence (including taking proper care and paying proper attention and diligence in the consideration of post-trade alerts or warnings) to promptly attend to cancellation of Market Transactions as required. This is also a critical measure in maintaining the integrity of a market;
- Only after a telephone call from the ASX, did Etrade through Etrade DTR 3 then request cancellation of the Relevant Transaction via email to the ASX. This email was sent approximately 50 minutes after the Relevant Transaction. Notwithstanding this, the ASX thereafter cancelled the Relevant Transaction under its direction;
- There was one breach of MIR 5.9.1;
- The misconduct was an isolated incident;
- Etrade did not derive any actual or potential benefit as a result of the misconduct;
- Etrade took steps to prevent recurrence of the breach, including:
    - Counselling Etrade DTR 1 in relation to the Relevant Order and managing ETF Orders in general;
    - Retraining all its DTRs on the management of ETF Orders; and
    - Reviewing and revising its DTR procedures.
- Etrade had no previous contraventions found against it by the MDP regarding non-compliance with the market integrity rules, but had previously been sanctioned by the ASX Disciplinary Tribunal on eight separate occasions since 2004 - one regarding the predecessor rule to MIR 5.9.1 that involved a DTR (ASX Circular 365/09 dated 30 October 2009);
- Etrade co-operated with ASIC throughout its investigation and did not dispute any material facts; and
- Etrade 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, Etrade has complied with the infringement notice, such compliance is not an admission of guilt or liability, and Etrade is not taken to have contravened subsection 798H(1) of the Corporations Act.

Further information on market integrity infringement notices, the market integrity rules or 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 "markets–supervision", "markets–market integrity rules" and "Markets Disciplinary Panel".