



ASIC

Australian Securities &
Investments Commission

Commonwealth of Australia Gazette

No. MDP09/16, Monday 21st November 2016

Published by ASIC

ASIC Gazette

Contents

Markets Disciplinary Panel Infringement Notice

Recipient: State One Stockbroking Ltd

The recipient has not complied with the infringement notice. The giving of an infringement notice to a recipient is only an allegation that the recipient has contravened subsection 798H(1) of the Corporations Act 2001, and the recipient is not taken to have contravened subsection 798H(1) of the Corporations Act 2001.

RIGHTS OF REVIEW

Recipients affected by the decision of the Markets Disciplinary Panel to give them an infringement notice under subsection 798H(1) of the *Corporations Act 2001* and Part 7.2A of the *Corporations Regulations 2001* administered by ASIC may have a right of review or may be entitled to have the infringement notice withdrawn. ASIC has published RG 216 to assist recipients to determine whether they have such rights – see RG 216.71 and RG 216.77 to 216.79. Copies of this document can be obtained from the ASIC website at www.asic.gov.au

ISSN 1445-6060 (Online version)
ISSN 1445-6079 (CD-ROM version)

Available from www.asic.gov.au
Email gazette.publisher@asic.gov.au

© Commonwealth of Australia, 2016

This work is copyright. Apart from any use permitted under the *Copyright Act 1968*, all rights are reserved. Requests for authorisation to reproduce, publish or communicate this work should be made to: Gazette Publisher, Australian Securities and Investment Commission, GPO Box 9827, Melbourne Vic 3001



PART 7.2A OF THE CORPORATIONS REGULATIONS 2001 INFRINGEMENT NOTICE

To: State One Stockbroking Ltd
Level 14, 172-176 St Georges Terrace
Perth WA 6000

TAKE NOTICE: The Australian Securities and Investments Commission ("ASIC") gives this infringement notice to State One Stockbroking Ltd ACN 092 989 083 ("State One") under regulation 7.2A.04 of the Corporations Regulations 2001 ("Regulations"). To comply with this notice State One must:

Pay a penalty to ASIC, on behalf of the Commonwealth, in the sum of **\$425,000**.

This infringement notice is given on 31 March 2016.

The unique code for this notice as required by paragraph 7.2A.06(b) of the Regulations is MDP17879/14.

The terms defined in Rule 1.4.3 of the ASIC Market Integrity Rules (ASX Market) 2010 have the same meaning when used in this notice, including those set out in the Appendix to this notice. Certain additional defined terms used in this notice are also set out in the Appendix to this notice.

Alleged contravention and penalty

State One was a Trading Participant in the Market operated by the ASX at the relevant time and was therefore an entity required by subsection 798H(1) of the *Corporations Act 2001* ("Act") to comply with the market integrity rules at that time.

State One is alleged to have contravened subsection 798H(1) of the Act by reason of contravening Rules 5.7.1 (b)(iii) and 5.5.2(b) of the ASIC Market Integrity Rules (ASX Market) 2010 ("MIR 5.7.1(b)(iii)" and "MIR 5.5.2(b)").

MIR 5.7.1(b)(iii) relevantly provides that:

"A Market Participant must not make a Bid or Offer for, or deal in, any Products...on account of any other person where...taking into account the circumstances of the Order, a Market Participant ought reasonably suspect that the person has placed the Order with the intention of creating a false or misleading appearance of active trading in any Product or with respect to the market for, or the price of, any Product."

MIR 5.5.2(b) relevantly provides that:

"A Trading Participant must have and maintain the necessary organisational and technical resources to ensure that...the Trading Participant complies at all times with these Rules and the Market Operating Rules"

On the evidence before it, the Markets Disciplinary Panel ("MDP") was satisfied that:

- 1) State One used an Automated Order Processing ("AOP") system to access the Trading Platform. State One allowed online clients to place Orders via the AOP system, resulting in either Bids or Offers, with the resultant trade being entered directly into the ASX Trading Platform.
- 2) Between 8 and 28 February 2011 a new client of State One ("Client") placed 141 Orders to buy fully paid ordinary shares in Tissue Therapies Limited ("TIS"), and amendments to those Orders (together "Initial Orders"), into State One's AOP system, pursuant to which State One entered 141 Bids and amendments to those Bids (together "Initial Bids"), into the ASX Trading Platform resulting in the execution of 189 Market Transactions for TIS.
- 3) The activity on the Client's account during this period showed that:
 - a) the Client had only traded in TIS, by buying it;
 - b) the Client had bought TIS on every Trading Day;
 - c) by the close of trading on 28 February 2011, the Client had bought 362,500 TIS at a total cost of \$221,475.58; and
 - d) the Client had transferred a further holding of 250,000 TIS to his State One account, such that he held a parcel of 612,500 TIS with State One, which was valued at \$416,500 at the beginning of trading on 1 March 2011.
- 4) During this period, on all but one Trading Day State One's SMARTS post-trade surveillance system generated 59 post-trade alerts relating to the entry and execution of the Initial Bids, including: driving the price of TIS; price ramping and creating a pattern of price driving.
- 5) A reasonable Market Participant would have: (a) identified the activity on the Client's account, as in 3 above; (b) performed a high level review of the Client's trading; (c) if that raised matters of concern, reviewed in detail at least the Client's most recent trading; and (d) made enquiries of the Client to determine the purpose of the trading.
- 6) A reasonable Market Participant would have identified that:
 - a) the Initial Orders resulted in the Client buying 13% of TIS sold on Market, but caused 88% of total price increases for TIS and 92% of late price increases;
 - b) the Client's trading was responsible for every price increase in TIS on 5 consecutive Trading Days and set the closing price for TIS on 11 of 15 or 73% of Trading Days; and
 - c) the Client often reduced the volume of his Bids when there were large volumes of TIS on offer and often amended the volume of his Bids to trade through price levels at minimum cost ("Volume Amendment Pattern").

- 7) A reasonable Market Participant would have identified that the Initial Orders that traded on 25 and 28 February 2011:
 - (a) appeared inconsistent with prior recent trading in TIS;
 - (b) materially altered the market for, or price of, TIS;
 - (c) appeared to have been timed to restore or increase the price of TIS;
 - (d) displayed the Volume Amendment Pattern;
 - (d) followed a pattern of starting as a resting Bid for 1,000 TIS low in priority in the Bid schedule and were amended shortly following a decrease in the price of TIS, or where an opportunity arose to trade through price levels in low volumes, transacting to cause a price increase, following which the Client entered a new resting Bid ("Timely Price Amendment Pattern"); and
 - (e) appeared to lack legitimate commercial reason.
- 8) State One did not contact the Client prior to 1 March 2011 to seek an explanation for his trading in TIS.
- 9) By the beginning of 1 March 2011 a reasonable Market Participant would have identified that the Initial Orders had materially altered the market for, or price of, TIS and formed two recognisable patterns of trading that were suggestive of price support. A reasonable Market Participant would also have reasonably suspected that the Client was placing Orders with the intention of creating a false or misleading appearance with respect to the market for, or price of, TIS.
- 10) On 1 and 2 March 2011 the Client placed three amendments to the Initial Orders, 17 new Orders to buy TIS and 13 amendments to those new Orders (together, "March Orders"). Pursuant to the March Orders, State One entered 33 Bids for TIS into the Trading Platform ("March Bids"), into the ASX Trading Platform resulting in the execution of 24 Market Transactions for TIS. The Clients Order exhibited the same characteristics as the Initial Orders.
- 11) Many of the March Orders and their execution were inconsistent with the recent trading in TIS because the average value of each Market Transaction was significantly lower than the average value of all transactions for TIS, indicating the Client was buying smaller volumes of TIS than average in each transaction.
- 12) A number of the March Orders and their execution materially altered the market for, or price of TIS, in that they: (a) caused 18 of 20, or 90% of all price increases in TIS; and (b) set the closing price for TIS on both days.
- 13) A number of the March Orders has an individual material effect on the market for or price of TIS.
- 14) Many of the March Orders appeared to have been timed to restore or increase the price of TIS, because of the March Bids that traded:
 - a) 10 were entered within one minute of a decrease in the price of TIS;
 - b) Two were entered within two minutes of a price decrease; and
 - c) Two were entered after the execution of a Market Transaction that left a small volume on offer at the priority Offer price such that the Client

traded through price levels, increasing the price of TIS at minimum cost.

15) The Client may have had an interest in creating a false or misleading appearance with respect to the market for, or price of, TIS because he held a large parcel of TIS.

16) A number of the March Orders appeared to constitute an unusual series of Orders, in that they displayed both the Volume Amendment Pattern and the Timely Price Amendment Pattern.

17) As a result of the Client not having resting Bids in the Market at close to priority price, the Client in effect negated any opportunity to acquire a substantial holding at minimum cost. Instead, the March Orders appeared to have been tailored to create price impact for minimum cost.

18) State One's SMARTS post-trade surveillance system generated 10 post-trade alerts relating to the entry and execution of the March Bids.

19) A reasonable Market Participant with knowledge of:

- a) the Client's history (including his TIS holdings);
- b) the Client's prior trading;
- c) the Client's patterns of trading; and
- d) the circumstances of each of the March Orders, as in 10-18 above,

would have suspected that the Client was placing those Orders with the intention of creating a false or misleading appearance with respect to the market for, or price of, TIS.

20) The Client continued to buy TIS through State One after 2 March 2011, purchasing small volumes and generating a disproportionate number of price increases.

21) ASIC made enquiries of State One on 15 April 2011 and 28 April 2011 in relation to its trading in TIS generally and the Client's account specifically.

22) On 18 April 2011, State One considered the Client's trading and concluded that he was not manipulating the market for TIS, but was a long-term buyer. On 10 May 2011, State One reviewed the Client's trading and formed the view that it was not comfortable with the Client's trading. State One closed the account on 1 February 2012.

23) Between 10 February and 9 May 2011, State One did not have and maintain policies and procedures structuring its employees' response to post-trade alerts. That one employee only received and reviewed the alerts did not excuse the failure.

By reason of State One's making Bids on behalf of the Client on 1 and 2 March 2011 in circumstances in which it ought reasonably have suspected that the Client placed the Orders with the intention of creating a false or misleading appearance with respect to the market for or price of TIS, the MDP has reasonable grounds to believe that State One contravened MIR 5.7.1(b)(iii), and thereby contravened subsection 798H(1) of the Act ("**Contravention 1**");

By reason of State One's failure between 10 February and 9 May 2011 to provide clear guidance to its employees responsible for reviewing post-trade alerts on what to do in the event of receiving post-trade alerts, the MDP has reasonable grounds to believe that State One contravened MIR 5.5.2(b), and thereby contravened subsection 798H(1) of the Act ("**Contravention 2**").

Maximum pecuniary penalty that a Court could order

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

- by reason of contravening MIR 5.7.1(b)(iii), is \$1,000,000;
- by reason of contravening MIR 5.5.2(b), is \$1,000,000.

The maximum pecuniary penalty that may be payable by State One under an infringement notice given pursuant to subsection 798K(2) of the Act:

- by reason of allegedly contravening MIR 5.7.1(b) (iii), is \$600,000;
- by reason of allegedly contravening MIR 5.5.2(b), is \$600,000.

Penalty under the Infringement Notice

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

- Contravention 1 - MIR 5.7.1(b)(iii) - \$275,000;
- Contravention 2 - MIR 5.5.2(b) - \$150,000.

Therefore, the total penalty that State One must pay to the Commonwealth is **\$425,000** being the penalty payable under this infringement notice for the two alleged contraventions of subsection 798H(1) of the Act.

The penalty is payable to ASIC on behalf of the Commonwealth. Payment is made by bank cheque to the order of the "Australian Securities and Investments Commission".

In determining this matter and the appropriate pecuniary penalty to be applied, the MDP took into account all relevant guidance, including ASIC Regulatory Guide 216-*Markets Disciplinary Panel*, and noted in particular the following:

- The remedies applied should:
 - promote market integrity and the confident and informed participation of investors in financial markets; and
 - act as a deterrent to any future misconduct by the subject person; and
 - also act as a general deterrent to others from engaging in the same or similar conduct;

- MIR 5.7.1(b) is aimed at upholding market integrity i.e. that markets remain fair and efficient. Protecting against market misconduct is designed to ensure that investors can be confident in making sound investment decisions. The overall objective is an active market that facilitates the capital formation important to national economic growth and prosperity;
- MIR 5.5.2(b) is also aimed at reinforcing the importance of having appropriate organisational and technical resources to uphold the integrity of the Market and to ensure the ASIC Market Integrity Rules and ASX Market Operating Rules are otherwise complied with;
- In the context of domestically licensed financial markets, the concept of market integrity is to be read in light of the objective in paragraph 760A(c) of the Act — 'to promote fair, orderly and transparent markets for financial products'. Fair, orderly and transparent means a level playing field (free from misconduct and synonymous with investor protection) characterised by sound ethical values and judgement where regular bids, offers and sales (past and real-time) can be seen and reflect genuine supply and demand;
- Making Bids and dealing in a Product absent the intent to take a genuine or bona fide position in the market for that Product, is significant for the reason that the resultant trading data creates a false and misleading appearance of supply, demand and/or liquidity and ultimately price or market valuation. Among other things, trading data is used by investors in making informed decisions by being able to assess supply, demand and/or liquidity and ultimately price or market valuation. False and misleading trading data thereby distorts a market and has the potential to undermine investor or public confidence in that financial markets are level playing fields and that prices reflect all available information. Accordingly, for these reasons, a breach of MIR 5.7.1(b)(iii) is of a very serious nature;
- Market Participants participate in the Market subject to the Act and ASIC Market Integrity Rules, with which they are required to comply. The responsibilities of Market Participants are not qualified by what ASIC itself might or might not detect about trading, and how it might or might not respond to what it detects. Market Participants cannot proceed upon any assumptions about the actions of ASIC, and must always consider their own obligations under the rules and act accordingly;
- There are no set parameters or definitive lists of potentially manipulative trading styles or approaches. Market Participants must consistently be on the lookout for subtle and novel ones, and for more than just typically employed methods of manipulation;
- Market Participants cannot invest in pre-trade filters and post-trade alert systems and rely on them to do all the work. Such systems have to be understood and analysed and acted upon in practice. Any post-trade alerts should be seen as the beginning and not the end of the process of surveillance of clients' trading. As such, Market Participants must have and maintain policies and procedures structuring their employee's response to alerts;

- The misconduct giving rise to Contravention 1 was reckless on the part of State One in its failure to comply with MIR 5.7.1(b)(iii). State One inappropriately claimed to take some comfort in ASIC's monitoring to relieve it of its obligations to comply with the ASIC Market Integrity Rules. State One inappropriately assumed a large volume of alerts were irrelevant, defeating their purpose. The predominantly Price Driver alerts showed that the Client's trading was out of line with other trading because of the disproportionate relationship between the percentage of total price increases as against the price of total volume of stock bought;
- State One failed to immediately contact the Client given the frequency of early alerts and having little information about the Client's history and intentions. State One failed to act, even after contact from ASIC. State One failed to identify clear signs of potentially manipulative trading, despite having the information available to do so. There is no doubt that the Volume Amendment Pattern and Timely Price Amendment Pattern could have been ascertained from a review of the information held by State One;
- The misconduct giving rise to Contravention 2 was negligent on the part of State One in its failure to comply with MIR 5.5.2. State One's policies and procedures did not provide clear guidance to its employees on how to read, understand and appropriately respond to post-trade alerts. State One did not have adequate backup for the Compliance Director or written procedures for when that person was unavailable. The Compliance Director effectively reported to himself;
- State One did not have a corporate culture conducive to compliance. State One assigned the role of reviewing post-trade alerts to its Compliance Director; however, that person had a poor understanding of potentially manipulative trading and a careless attitude to its prevention. The Compliance Director also lacked understanding of the alerts and the information more generally available in State One's systems. State One formed a view (and persisted with it) that the Client's motivation was merely accumulation, which was not substantiated by the objective evidence. State One inadequately recorded its assessment of the Client's trading and why it did not act. Despite State One forming the view on 10 May 2011, it did not close the Client account until 1 February 2012;
- There was one breach of MIR 5.7.1(b)(iii) and one breach of MIR 5.5.2(b) alleged;
- While the alleged breach of MIR 5.5.2(b) may have contributed to that of MIR 5.7.1(b)(iii), they were distinct. The breaches, especially in combination, indicated systemic compliance failure;
- The alleged breaches were of a very serious nature;
- State One also did not self-report the breaches as required under section 912D of the Act;
- The alleged breach of MIR 5.5.2(b) occurred over about three months. This was an unacceptably long period. The alleged breach of MIR 5.7.1(b)(iii) occurred over two days. Manipulative trading for any period of time is significant;

- There was no specific benefit to State One. However, the potential for detriment was real and apparent. As a result of State One's failure to identify the Client's trading as potentially manipulative, the Client was able to materially alter the price for TIS during the two days, and in particular the closing prices. Closing prices provide a daily reference point and are used by investors to make informed investment decisions. Manipulation of closing prices is especially egregious. State One's facilitation of the Client's conduct created an unfair and inefficient market, and consequently negatively impacted on the integrity of the Market and risked undermining confidence in the Market and its orderly operation;
- State One's failure to provide clear guidance to employees on responding to post-trade alerts diminished its ability to effectively detect and stop potentially manipulative trading by its clients. This had the very real capacity to interfere with the fairness and efficiency of the Market, and engender trading that did not reflect genuine supply and demand. Again, this misconduct risked public confidence in the Market;
- State One took remedial steps to prevent recurrent breaches including to:
 - creating a new Market Surveillance Team;
 - employing a Market Surveillance Officer;
 - employing an Operations Manager, with responsibility to oversee the Market Surveillance Team;
 - preparing a new and improved Compliance Procedure manual;
 - preparing a Responsible Executive Regime and Management Plan;
 - carrying out a review of all policies and procedures;
 - updating its Market Integrity Obligation forms;
 - creating a new Online Application Form which incorporates an Online Trading Market Integrity Agreement;
 - updating its DTR policy to include procedures in relation to the operation of SMARTS and to bring alerts to the attention of others' employees;
 - appointing 3 additional Designated Trading Representatives;
 - subscribing to additional SMARTS subscriptions; and
 - adding the Chi-X Market to the SMARTS subscription.
- While these were positive remedial steps, they came years after the alleged breaches, the same person remained the Compliance Director and the improved structure had not led State One to reassess its attitude to the Client's trading and acknowledge its failures;
- State One had no prior contraventions found against it by the MDP, but had been sanctioned by the ASX Disciplinary Tribunal and Appeal Tribunal on 2 occasions.

In 2006 a penalty of \$15,000 was imposed upon State One for failing to maintain appropriate records and transaction approval policies. In 2009 a penalty of \$235,000 was imposed upon State One for contraventions of ASX Market Rules 13.4.1(a), 4.1.1(w) and 13.4.1 (being the predecessor rule to MIR 5.7.1). State One's compliance history was unsatisfactory. These matters suggested an ongoing failure to recognise its compliance and regulatory obligations. The 2009 matter in particular, (though related to

trading as Principal), should have put State One on alert for potentially manipulative trading and ensured it acted to prevent such trading.

Compliance with the Infringement Notice

State One may choose not to comply with this infringement notice, but if State One does not comply, civil proceedings may be brought against State One in relation to the alleged contraventions.

To comply with this infringement notice, State One must pay the penalty within the compliance period. The compliance period:

- (a) starts on the day on which the infringement notice is given to State One; and
- (b) ends 27 days after the day on which the infringement notice is given to State One;

unless an application is made for its extension.

State One may apply to ASIC for an extension of time to comply with this notice under regulation 7.2A.09 of the Regulations. If State One does so, and the application is granted, the compliance period ends at the end of the further period allowed.

If State One applies for a further period of time in which to comply with this notice, and the application is refused, the compliance period ends on the later of:

- (a) 28 days after the day on which the infringement notice was given to State One; and
- (b) 7 days after the notice of refusal is given to State One.

State One may apply to ASIC for withdrawal of this notice under regulation 7.2A.11 of the Regulations. If State One does so, and the application is refused, the compliance period ends 28 days after the notice of refusal is given to State One.

Effect of issue and compliance with the Infringement Notice

The effects of compliance with this infringement notice are:

- (a) any liability of State One to the Commonwealth for the alleged contraventions of subsection 798H(1) of the Act is discharged;
- (b) no civil or criminal proceedings may be brought or continued by the Commonwealth against State One for the conduct specified in the infringement notice as being the conduct that made up the alleged contraventions of subsection 798H(1) of the Act;
- (c) no administrative action may be taken by ASIC under section 914A, 915B, 915C or 920A of the Act against State One for the conduct specified in the infringement notice as being the conduct that made up the alleged contraventions of subsection 798H(1) of the Act;
- (d) State One is not taken to have admitted guilt or liability in relation to the alleged contraventions; and,
- (e) State One is not taken to have contravened subsection 798H(1) of the Act.

Publication

ASIC may publish details of this infringement notice under regulation 7.2A.15 of the Regulations.

**Susan Humphreys**

Counsel to the Markets Disciplinary Panel
with the authority of a Division of the Australian Securities & Investments Commission

Dated: 31 March 2016

Note: Members of the Markets Disciplinary Panel constitute a Division of ASIC as delegates of the members of the Division for the purposes of considering the allegations covered by this notice.

Appendix - Defined Terms

The terms defined in MIR 1.4.3 have the same meaning when used in this notice, including:

"ASX" means ASX Limited (ACN 008 624 691).

"Automated Order Processing" ("AOP") means the process by which orders are registered in a Trading Participant's system, and, if accepted for submission into a Trading Platform by the Trading Participant submitted as a corresponding Trading Message without being keyed or rekeyed by a Designated Trading Representative ("DTR").

"Bid" relevantly means a price and quantity of the Cash Market Product to be purchased.

"Cash Market Product" means any product that the Market Operator authorises for trading on a Trading Platform as a Cash Market Product.

"DTR" means a Representative of the Trading Participant who has been authorized by the Trading Participant to submit Trading Messages to the Trading Platform on behalf of the Trading Participant.

"Market" means the market operated by the Market Operator under Australian Market Licence (Australian Stock Exchange Limited) 2002.

"Market Operator" means ASX Limited.

"Market Participant" means a Participant in the Market admitted under the Market Operating Rules.

"Market Transaction" means a transaction for one or more Products, entered into on a Trading Platform or reported to the Market Operator under the relevant operating rules.

"Offer" relevantly means a price and quantity of the Cash Market Products to be sold.

"Product" relevantly includes a Cash Market Product.

"Order" relevantly means an instruction to purchase or sell Cash Market Products, or an instruction to amend or cancel a prior instruction to purchase or sell Cash Market Products.

"Trading Day" means a day on which Market Transactions may be entered into by Trading Participants on a Trading Platform.

"Trading Messages" means those messages submitted into a Trading Platform relating to trading functions, such as Orders, amendment or cancellation of Orders and the reporting or cancellation of Market Transactions on the Trading Platform.

"Trading Participant" means a Market Participant which has Trading Permission in respect of one or more Products.

"Trading Permission" means the right to submit Trading Messages in a Trading Platform.

"Trading Platform" means a facility made available by the Market Operator to Trading Participants for the entry of Trading Messages, the matching of Orders, the advertisement of invitations to trade and the reporting of transactions.

This notice adopts the following additional definitions of terms:

"SMARTS" means SMARTS.Broker, Credit Suisse's post-trade surveillance system.