



ASIC

Australian Securities & Investments Commission

REPORT 405

ASIC supervision of markets and participants: January to June 2014

August 2014

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 January to 30 June 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 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

Contents

Overview.....	4
ASIC supervision of markets and participants.....	4
Purpose and scope of this report.....	5
Achieving positive behavioural change	5
Significant outcomes for the relevant period	8
Future areas of focus.....	10
The role of gatekeepers.....	12
A Market surveillance	14
Real-time surveillance of Australia's licensed financial markets	14
Market enquiries	15
Other surveillance activities	16
B Supervision of market participants and securities dealers	18
Compliance activity	18
Referrals about market participants.....	22
Self-reporting to ASIC.....	22
Engagement with ASIC.....	23
C Market enforcement outcomes	24
Investigation and enforcement outcomes.....	24
Examples of ASIC enforcement outcomes.....	25
Markets Disciplinary Panel	29
Appendix: Schedule of media releases	32
Key terms	33

Overview

ASIC supervision of markets and participants

- 1 The Australian Securities and Investments Commission (ASIC) is Australia's corporate, markets and financial services regulator. As markets regulator, we are responsible for the supervision of trading on Australia's domestic licensed equity, derivatives and futures markets.
- 2 Our core priority for markets is the promotion of investor confidence through fair and efficient markets. This requires market infrastructure that is robust, where the trading, clearing and settlement of transactions is orderly and efficient, and where market misconduct is minimised.
- 3 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 meet their Australian financial services (AFS) licence conditions: see Section B.
- 4 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.
- 5 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 9–19.

Purpose and scope of this report

- 6 This report summarises key operational statistics and outcomes achieved by ASIC in relation to ASX, ASX 24 and Chi-X for the period 1 January to 30 June 2014.
- 7 It also highlights markets-related enforcement outcomes that were achieved by ASIC during this period. A comprehensive account of our enforcement activities over this time is set out in Report 402 *ASIC Enforcement outcomes: January to June 2014* (REP 402).
- 8 This is the eighth of ASIC's six-monthly market supervision reports. Previous reports are available at: www.asic.gov.au/reports.

Achieving positive behavioural change

- 9 Achieving positive behavioural change is an important part of our work as market regulator. Through early intervention, we may be able to prevent potential breaches of the Corporations Act or market integrity rules—and consequential investor losses—before they occur.
- 10 The types of conduct we target for positive behavioural change are activities that, without regulatory intervention, may 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 of the Corporations Act or market integrity rules is not just a suitable candidate for positive behavioural change, but may also be subject to ASIC enforcement action. This approach will also not be considered for serious market misconduct matters.
- 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.

Direct engagement

- 13 We maintain an active dialogue with market participants to address compliance concerns. For example, between 1 January and 30 June 2014 (the relevant period), discussions with market participants led to the amendment of order execution methods and review of trading algorithms on 30 occasions: see Table 4.
- 14 Our market surveillance activities occasionally reveal unusual trading patterns which may be indicative of potential market misconduct. As part of

our early engagement process, we regularly meet with market participants (including fund managers, hedge funds and individual traders) to raise our concerns about such behaviour: see Example 1.

Example 1: Early engagement to discuss concerns

In the relevant period, we met with a fund manager to raise our concerns regarding trading behaviour involving unusual price movements caused by small trading volumes. Following the meeting, we closely monitored trading by the fund in question and noted that this behaviour had ceased.

Risk assessments

- 15 Through our risk assessment program for market participants, we are able to:
- (a) gather intelligence for information and assessment purposes;
 - (b) assess the risks associated with a market participant's business;
 - (c) identify any weaknesses or concerns in relation to a market participant's business;
 - (d) raise a market participant's awareness of its obligations; and
 - (e) highlight ASIC's current areas of focus.
- 16 After conducting a risk assessment, we may send the market participant involved a letter containing our observations and recommendations. These letters can include suggestions for improving compliance where we have identified concerns. On many occasions, this has led to improvements in market participants' compliance frameworks and increased awareness of their compliance obligations and impacts of recent regulatory changes on their businesses.

Warning letters

- 17 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.
- 18 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.

Example 2: Warning letters

Warning letters from ASIC may include the following statements:

- 'If any further material evidence in relation to this matter comes to ASIC's attention, ASIC reserves the right to re-open its investigation into this matter and take some other action, including referring the matter to the MDP.'
- 'Further, while we consider an appropriate regulatory outcome is achieved on this occasion, should your future conduct raise similar issues to those in evidence in this matter, ASIC reserves the right to refer to this letter in any future MDP proceedings as a relevant factor to be considered by the MDP in determining penalty.'

Publications for industry

19 Throughout 2014, we have published regular *Market supervision updates* (MSUs), highlighting current issues in market supervision and surveillance, including changes to market integrity rules and compliance issues: see Figure 1. 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, at www.asic.gov.au/ASIC-market-supervision-update.

Figure 1: *Market supervision update—Issue 45, April 2014*



Significant outcomes for the relevant period

Market surveillance

- 20 In the relevant period, we conducted a total of 122 market surveillance enquiries of equities and futures participants, including reactive, proactive and targeted surveillances.
- 21 We have continued 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. We recently developed a new insider trading report in MAI that looks at ASX equities and derivatives data in far greater detail than the previous system allowed for.
- 22 Further details of our surveillance activities (including MAI) can be found in Section A.

Supervision of market participants and securities dealers

- 23 In the relevant period, we completed 35 risk-based assessment visits. As a result of these assessments, we recommended that some market participants and securities dealers review and enhance their supervisory arrangements, taking into consideration the nature, scale and geographical distribution of their business.
- 24 In addition, 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.
- 25 Further details of our supervision activities can be found in Section B.

Market enforcement outcomes

- 26 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)	✓		✓	✓
Continuous disclosure (2)	✓	✓	✓	✓
Market manipulation (1)	✓		✓	✓
Infringement notices (8)	✓	✓	✓	✓
Other sanctions (1)	✓	✓	✓	✓

- 27 The Market Integrity Enforcement team typically had over 80 matters under investigation at any one time during the relevant period. In carrying out these investigations, ASIC's investigation powers were used to conduct 66 formal interviews with persons of interest, issue 326 notices to obtain information and execute four search warrants in collaboration with the Australian Federal Police (AFP).
- 28 Appropriate handling of confidential information is essential to ensuring all investors are trading on the same information. We 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.
- 29 A significant enforcement outcome for ASIC, and investor confidence more broadly, was the \$1.2 million penalty imposed by the Federal Court on Newcrest Mining Limited (Newcrest) for contravening its continuous disclosure obligations: see Example 3. This is the highest civil penalty awarded in Australia for a continuous disclosure matter and was obtained just over 12 months after the relevant conduct occurred. This outcome serves as a reminder to all listed entities of the importance of appropriate handling of market-sensitive information.

Example 3: Selective disclosure of market-sensitive information

The Federal Court imposed a \$1.2 million penalty on Newcrest for contravening its continuous disclosure obligations by briefing analysts on market-sensitive information ahead of it being disclosed to the market.

From 28 May 2013, in a series of briefings to analysts, Newcrest disclosed its expected gold production for the 2013–14 financial year. On 5 June 2013, Newcrest disclosed information to analysts regarding its expected capital expenditure for the 2013–14 financial year.

As this information was market sensitive and selectively disclosed to analysts, Newcrest was obliged to disclose this information to ASX. We

alleged Newcrest's contraventions continued until 7 June 2013, when it made an announcement to ASX which included its 2013–14 expected gold production, capital expenditure and other matters, including write downs.

Newcrest admitted the contraventions and the parties filed a joint application for civil penalties to be imposed.

The court heard a joint submission from ASIC and Newcrest as to the appropriate penalties. The parties jointly proposed a penalty of \$800,000 for the first contravention (relating to the expected gold production for the 2013–14 financial year), and \$400,000 for the second contravention (relating to the expected capital expenditure for the 2013–14 financial year).

The court accepted these submissions.

Our investigation in relation to persons who received this information is ongoing.

- 30 Further details of our markets enforcement outcomes can be found in Section C.

Guidance and reports

- 31 As well as our regular MSUs (see paragraph 19) we have released a number of reports addressing markets issues. For example:
- (a) In April 2014, we released our submission to the 2014 Financial System Inquiry (Murray Inquiry). Our submission addressed a range of markets-related issues, including high-frequency trading, automation and sophistication of trading technology, the regulation of securities dealers and financial markets infrastructure.
 - (b) In May 2014, we released the results of a review of rule changes affecting dark trading and their impact on market quality: see Report 394 *Review of recent rule changes affecting dark liquidity* (REP 394). Our review indicated that trends in dark liquidity that were previously of some concern have discontinued. We will continue to monitor and respond to the challenges posed by changing market dynamics and technical advancements, particularly in respect of high-frequency trading and dark pools.

Future areas of focus

Handling of confidential information

- 32 ASIC is eager to raise industry standards in relation to the treatment of confidential information by listed companies. We have been 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.

- 33 In May 2014, we released a report on the handling of confidential information: see Report 393 *Handling of confidential information: Briefings and unannounced corporate transactions* (REP 393). We are currently monitoring changes to research analyst ratings to identify whether selective briefings are occurring. A focus of our risk assessment visits in the coming six-month period will be the handling of confidential information and supervisory arrangements for research analysts. Where we identify inappropriate disclosures, we will take enforcement action: see Example 3.

Designated trading representatives

Orders rejected by system filters

- 34 The majority of trading orders in Australian are transmitted to financial markets electronically. 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.
- 35 Our Market Surveillance team continues to encounter issues with automated trade filters and trading anomalies associated with DTR execution of orders that have been rejected by system filters. We have observed instances where DTRs are entering these orders without first considering the subsequent market impact.
- 36 Market participants must ensure that they have appropriate system controls and filters in place for trades they execute electronically. In particular, participants should ensure that DTRs have due regard for the consequences of their actions at all times. We will continue to monitor the market for occurrences of this conduct.

'Fat finger' errors

- 37 We are concerned about the ongoing incidence of erroneous entries of orders that affect the market, often referred to as 'fat finger' errors. These errors have the potential to damage the integrity and reputation of the market.
- 38 Alleged breaches of Rule 5.9.1 of the ASIC Market Integrity Rules (ASX Market) 2010 represent 41% of all matters referred to the MDP for determination. Not all of these relate to 'fat finger' errors. However, these errors continue to be over-represented, including in matters currently being investigated by ASIC's Market Integrity Enforcement team.

Note: In this document 'ASIC Market Integrity Rules (ASX)' refers to the ASIC Market Integrity Rules (ASX Market) 2010 and 'ASIC Market Integrity Rules (Chi-X)' refers to the ASIC Market Integrity Rules (Chi-X Australia Market) 2011.

- 39 Inadvertent human error by a DTR is often blamed for these errors. We have advised industry that we have little tolerance for this excuse and will be taking a harder line against this conduct in coming months.

Principal trading and client facilitation

- 40 In the relevant period, we met with a number of market participants who engage in principal trading and client facilitation, to determine:
- (a) the nature and extent of their facilitation and principal trading activities in Australia;
 - (b) who undertakes principal trading and facilitation activities; and
 - (c) arrangements for managing information flows and conflicts of interest.
- 41 In the coming months, we will provide updates and feedback on our review of principal trading and facilitation activities.

Suspicious activity reporting

- 42 Participants of the ASX and Chi-X markets must notify ASIC if they have reasonable grounds to suspect that a person has placed an order or entered into a transaction while in possession of inside information, or which has the effect of creating or maintaining an artificial price or a false or misleading appearance in the market or price for trading in financial products: see Rule 5.1.11 of the ASIC Market Integrity Rules (ASX) and Rule 5.1.11 of the ASIC Market Integrity Rules (Chi-X).
- 43 The majority of market participants did not submit any suspicious activity reports in the relevant period. To ensure compliance with this obligation, we will inspect breach registers of market participants as part of our compliance program. We will also consider whether matters that come to our attention in other ways should have been reported under Part 5.11 of the ASIC Market Integrity Rules (ASX) or Part 5.11 of the ASIC Market Integrity Rules (Chi-X).

The role of gatekeepers

- 44 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.
- 45 Market licensees, market participants and securities dealers 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.

46 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

- 47 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

- 48 Our supervision of financial markets has been strengthened by the successful rollout of our new market surveillance system, MAI. MAI was purpose-built and designed to handle the dynamic nature of Australia's financial markets. MAI enables us to examine very large data sets and review granular information on the behaviour of high-frequency trading and algorithmic traders.
- 49 MAI system developments during the relevant period have enabled ASIC surveillance analysts to more fully examine historical trading data to more quickly identify anomalous trading activity that may require investigation. As noted at paragraph 21, 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.

Trade surveillance reports

- 50 Trade surveillance alerts are indicators of unusual trading activity. During the relevant period, there were 17,091 alerts, compared to 19,255 alerts in the previous period: see Table 2.
- 51 In general, the overall number of alerts generated in any one period is affected by a number of factors, including general market volatility, the level of corporate transactions and general trading conditions. In this instance, however, the reduction in alert numbers is due to our continuing calibration of MAI to exclude alerts that are explainable and non-problematic. We expect that future MAI enhancements will lead to even greater refinement and calibration of alerts and reports, resulting in further efficiencies.

Table 2: Trade surveillance alerts

Surveillance activity	Previous periods		Relevant period
	1 Jan–30 June 2013	1 July–31 Dec 2013	1 Jan–30 June 2014
Total number of alerts	20,938	19,255	17,091

Derivatives surveillance

- 52 In November 2013, we established a dedicated Derivatives Surveillance team. Together with the MAI system enhancements, this has changed the way we undertake derivatives surveillance. Where previously surveillance analysts would manually examine spreadsheets, MAI has largely automated this process. We are now able to examine extended trading periods in greater depth, for example, by looking at individual participant accounts.

Market enquiries

- 53 When our surveillance analysts are not able to explain an alert or series of alerts by reference to available market information (including media, internet chat sites, broker research and dialogue with brokers), we may conduct market enquiries. Not all enquiries result from MAI alerts. Enquiries may also be 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 73–80.
- 54 We may call on market participants 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.
- 55 The number of enquiries undertaken in the relevant period rose for the third consecutive period: see Table 3. There were 122 enquiries undertaken during the relevant period, compared with 102 in the previous period. The majority of these enquiries related to insider trading and are largely attributable to rising takeover activity in the Australian market. Increased activity by our new Derivatives Surveillance team also contributed to the overall increase in enquiry numbers.
- 56 Continuous disclosure enquiries are generated by ASIC surveillance analysts as well as referrals from ASX: see paragraph 72. The number of continuous disclosure-related enquiries remained steady. However, the number of enquiries relating to breaches of market integrity rules increased—this was, in part, due to derivatives market statistics now being included in this category.

Table 3: Markets enquiries

Alleged offence	Previous periods		Relevant period
	1 Jan–30 June 2013	1 July–31 Dec 2013	1 Jan–30 June 2014
Insider trading	51	53	51
Market manipulation	23	21	32
Continuous disclosure	9	13	14
Breach of market integrity rules	11	15	25
Total	94	102	122

57 In the relevant period, ASIC's Market and Participant Supervision (MPS) team referred a total of 21 matters to the Market Integrity Enforcement team for investigation. This included 11 referrals for conduct involving suspected insider trading and four referrals for conduct involving suspected continuous disclosure breaches. The number of referrals is consistent with the previous corresponding period.

Other surveillance activities

58 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.

59 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 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.

60 Market participants are responsible for ensuring that their technology systems are appropriate. This includes the 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

Surveillance activities	Previous periods		Relevant period
	1 Jan–30 June 2013	1 July–31 Dec 2013	1 Jan–30 June 2014
Execution strategy	7	11	17
Algorithmic trading and filter issues	6	7	9
Other	6	8	4
Total	19	26	30

Reporting markets or trading issues

61 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 using 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

- 62 Risk-based assessments of all market participants are conducted by ASIC on a rolling basis. In the relevant period, we completed 35 risk-based assessments of participants, up from 17 in the previous period. This increase is due to a number of reviews that were commenced in the previous period before being completed in the relevant period.
- 63 Risk-based assessments focus on the risks associated with a market participant's business. This helps us to identify any weaknesses or concerns in relation to the participant's business. It is also an opportunity for us to highlight ASIC's current areas of focus, raise the participant's awareness of their obligations and gather intelligence for information and assessment purposes.
- 64 Engagement with industry through presentations and liaison meetings further develops our relationships with market participants and provides information on topical issues and potential risks facing the industry. During the relevant period, we undertook 17 industry presentations on markets-related issues: see Table 5.

Compliance reviews

- 65 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 55 participant compliance reviews, compared with 73 for the previous period. This decrease is due to internal restructuring (i.e. some of the matters that were previously included in this figure are now dealt with by the new Derivatives Surveillance team): see paragraph 52. The underlying number of compliance reviews carried out has remained broadly unchanged.
- 66 In our compliance reviews we noted that there were some shortcomings in the monitoring and supervision of DTRs and advisers due to non-compliance with procedures, insufficient resources and a lack of oversight in regional or

branch offices. We are currently working 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.

- 67 Our compliance reviews also identified deficiencies involving the provision of personal advice and the requirement to provide a clear, concise and effective Statement of Advice (SOA). For example, we identified market participants that had not provided sufficient information to the client regarding the basis on which the advice was given. We also identified instances where generic statements were used for all or several clients. This suggests that inadequate consideration may have been given to the client's circumstances, goals and objectives.
- 68 In compliance reviews of managed discretionary accounts we looked for 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 we provided additional guidance to help ensure that participants' obligations were met.
- 69 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 16. 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 Jan–30 June 2013			1 July–31 Dec 2013			1 Jan–30 June 2014			
	Outstanding (1 Jan 2013)	New	Completed	Outstanding (30 Jul 2013)	New	Completed	Outstanding (31 Dec 2013)	New	Completed	Outstanding (30 Jun 2014)
Compliance reviews (includes business-as-usual equities and futures participants, reactive, proactive and targeted)	70	77	88	59	66	73	52	31	55	28
Monitoring and remediation	7	3	6	4	1	1	4	2	4	2
Risk-based assessment visits	7	47	45	9	18	17*	10	25	35	–
Other (e.g. industry presentations)	–	20	20	–	22	22	–	17	17	–

* This figure has been revised upward from 16 to 17 following the identification of an additional review in the relevant period.

70 Table 6 shows that 11 AOP certifications were received in the relevant period. Although this figure is lower than the previous period, we note that the number of AOP certifications received by ASIC in any given period is driven by market participants.

71 Applications and notifications to ASIC in the relevant period included the renewal of accredited derivatives advisers (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.

DRAFT

Table 6: Applications, waivers, notifications and exemptions

Applications, waivers, notifications and exemptions	Previous periods						Relevant period			
	1 Jan–30 June 2013			1 July–31 Dec 2013			1 Jan–30 June 2014			
	Outstanding (1 Jan 2013)	New	Completed	Outstanding (30 Jul 2013)	New	Completed	Outstanding (31 Dec 2013)	New	Completed	Outstanding (30 Jun 2014)
Applications	1	275	273	3	84	83	4	90	93	1
Waivers requested (ASX)	–	–	–	–	8	7	1	2	2	1
Waivers requested (ASX 24)	1	–	1	–	5	3	2	–	2	–
Waivers requested (Chi-X)	–	–	–	–	5	5	–	1	1	–
Waivers requested (NSX)	–	1	1	–	–	–	–	–	–	–
Waivers requested (Competition)	–	13	13	–	5	5	–	2	2	–
Waivers requested (APX)	–	–	–	–	–	–	–	3	1	2
Relief applications	4	9	9	4	11	14	1	3	4	–
AOP certifications received (includes significant changes)	6	27	31	2	23	23	2	11	13	–
Notifications (includes professional indemnity insurance, responsible executive changes and ADA withdrawals)	10	226	229	7	314	302	19	151	154	16

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.

DRAFT

Referrals about market participants

- 72 The following referrals about market participants were received by ASIC in the relevant period:
- (a) five 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) 10 referrals were received from ASX in relation to continuous disclosure activities; and
 - (d) six referrals were received from ASX in relation to participant misconduct issues such as AOP and filter or trust account issues.
- 73 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

- 74 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. This is an area where we expect to see stronger action from industry in the future.
- 75 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).
- 76 In the relevant period, we received 22 breach notifications from market participants, of these:
- (a) seven breaches of the Corporations Act were self-reported by market participants;
 - (b) seven breaches of market integrity rules were self-reported by market participants; and
 - (c) eight breaches of both the Corporations Act and market integrity rules were self-reported by market participants.

- 77 In addition, 12 trust account notifications were made under market integrity rules by market participants.
- 78 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

- 79 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.
- 80 We encourage market participants to raise any trading issues or concerns with us at an early stage. The MPS team may be contacted using the hotline or 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 and a comparison of two-year periods since 2010. Given the time it takes to identify and investigate cases, we consider that a two-year reporting period provides a clearer indication of trends in enforcement outcomes.

Investigation and enforcement outcomes

- 81 Enforcement action is about punishing wrongdoing and, as importantly, 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, in which the outcome is often ultimately contingent on the availability of evidence. For this reason, we seek to maximise the deterrence value of all our enforcement activities.
- 82 Table 7 outlines significant market enforcement outcomes for the two-year period 1 July 2012 to 30 June 2014, compared to the preceding two-year period ending 30 June 2012. It includes a 'snapshot' of the outcomes for the current six-month period ending on 30 June 2014.

Table 7: Investigation and enforcement outcomes

Significant market integrity related outcomes	Previous two-year period	Current two-year period	
	1 July 2010–30 June 2012 (two years)	1 July 2012–30 June 2014 (two years)	1 Jan–30 June 2014 (six months)
Bannings	2	1	–
Insider trading pleas, verdicts and judgements	5	20	3
Continuous disclosure infringement notices	7	6	2
Other sanctions (enforceable undertakings and pecuniary penalties)	6	13	1
Market manipulation pleas, verdicts and judgements	3	2	1

Significant market integrity related outcomes	Previous two-year period	Current two-year period	
	1 July 2010–30 June 2012 (two years)	1 July 2012–30 June 2014 (two years)	1 Jan–30 June 2014 (six months)
Infringement notices issued by the MDP	4*	24	8
Total	27	66	15

* The MDP was established in July 2010, however, no matters were referred to it for decision until 2011.

Examples of ASIC enforcement outcomes

Insider trading

- 83 Insider trading is a form of theft and will not be tolerated.
- 84 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.
- 85 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.
- 86 In the relevant period, we achieved three enforcement outcomes against individuals for insider trading activity: see Example 4.

Example 4:



- 87 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.
- 88 We expect company boards and investors to fulfil their obligation to ensure compliance with insider trading laws. We also expect them to consider the acceptability of conduct that does not breach the law but which may have an effect on investor confidence.
- 89 ASIC's role is to thoroughly investigate potential insider trading breaches and, where sufficient evidence exists, take enforcement action to uphold insider trading laws. In addition, we facilitate discussions with industry and companies in relation to legal requirements and best practice. For example, earlier this year, we hosted a roundtable discussion on specific governance issues, including directors trading.

Inter-agency cooperation

- 90 A joint operation was launched by ASIC and the AFP after suspicious trading in foreign exchange derivatives was identified. The AFP and ASIC worked closely together on this serious and complex investigation, utilising the resources and expertise of both agencies, ultimately leading to the arrest of two men: see Example 5.
- 91 Investigations like this send a clear message to anyone who is thinking of engaging in this type of criminal activity—we have the ability to monitor wrongdoing and take action.

Example 5: Insider trading and abuse of public office

Two men were arrested by the AFP for offences relating to insider trading, money laundering, corruption and abuse of public office. The arrests were the result of a joint AFP and ASIC operation after suspicious trading in foreign exchange derivatives was identified and monitored.

Authorities discovered that a 26-year-old man, an employee of the National Australia Bank (NAB), appeared to be receiving sensitive information from a 24-year old man, an employee of the Australian Bureau of Statistics (ABS). It will be alleged in court that the 26-year-old man was obtaining this market-sensitive information before its official release by the ABS, then using it to enter into foreign exchange derivative products and personally profit from favourable movements in the prices of those derivatives.

This trading activity, occurring between August 2013 and May 2014, resulted in profits of approximately \$7 million. Both the NAB and the ABS provided their full cooperation and assistance to police throughout the investigation.

Market manipulation

92 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.

93 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:



Continuous disclosure breaches

94 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.

95 Broadly speaking, we consider that there is good compliance with the continuous disclosure obligations in Australia. We take very few actions relative to the number of announcements made, and far fewer than market commentators say 'must' be breaches.

- 96 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.
- 97 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 awarded in Australia for a continuous disclosure breach was imposed on Newcrest, following an ASIC investigation: see Example 3.

Example 7: Continuous disclosure infringement notice

On 4 December 2012, Diploma Group Limited (DGX) entered into a contract for the sale of 69 Adelaide Terrace, East Perth, for \$4.86 million. The contract was subject to two conditions:

- due diligence and syndicate funding approval; and
- development approval.

DGX did not announce the entering of the contract, but waited until 31 July 2013 to announce the settlement. The announcement included the following statements:

- 'The sale of this asset places the business in a stronger position financially having reduced corporate debt by close to 30% to \$13 million.'
- 'Diploma will recognise a profit from the sale in the first half of FY14.'

ASIC alleged that by failing to inform ASX of its entry into the contract for the sale of the property subject to the two conditions, DGX was in breach of s674(2) of the Corporations Act.

DGX paid a penalty of \$33,000 after ASIC served an infringement notice on the company for failing to comply with its continuous disclosure obligations. DXG is not, by reason of its compliance with the infringement notice, regarded as having contravened s674(2) of the Corporations Act.

Enforceable undertakings

- 98 ASIC pursues negotiated outcomes (which may arise from surveillances or from 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.
- 99 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

In November 2012, BNP Paribas (BNP) reported to ASIC that it had identified conduct that occurred between 2007 and 2010 that was indicative of seeking to influence its Australian Bank Bill Swap Rate (BBSW) submissions, based on how the submissions may benefit BNP's derivatives positions. BNP remained a member of the BBSW submissions panel until a new methodology for calculating the BBSW was implemented on 27 September 2013.

ASIC accepted an enforceable undertaking from BNP in relation to potential misconduct involving the BBSW. BNP will also make a voluntary contribution of \$1 million to fund independent financial literacy projects in Australia.

The enforceable undertaking requires BNP to ensure its participation in relation to the setting of Australian interest rate benchmarks upholds the integrity and reliability of those benchmarks. At ASIC's request, BNP engaged an independent expert to conduct a review of BBSW submissions. The expert found that any market impact was not significant.

Since November 2012, BNP has fully cooperated with ASIC in relation to ASIC's investigation into the reported conduct. ASIC acknowledges BNP's cooperation and assistance in regard to its investigation, and that BNP self-reported this matter to ASIC. ASIC's enquiries in relation to the BBSW submission process and rate set are ongoing.

Note: Our policy regarding enforceable undertakings is contained in Regulatory Guide 100 *Enforceable undertakings* (RG 100). Copies of enforceable undertakings are available from the ASIC website at www.asic.gov.au/euregister.

Markets Disciplinary Panel

- 100 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.
- 101 In the relevant period, the MDP issued eight infringement notices for contraventions of market integrity rules, all of which were complied with. These were:
- (a) Citigroup Global Markets Australia Pty Limited 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 ([14-009MR](#)) *Citigroup Global Markets Australia Pty Limited pays \$40,000 infringement notice penalty* (21 January 2014).

- (b) Pershing Securities Australia Pty Ltd paid a penalty of \$15,000 to comply with an infringement notice given to it by the MDP. The penalty was for failing to give confirmations to retail clients for market transactions entered into on the retail clients' instructions: see Media Release ([14-019MR](#)) *Pershing Securities Australia Pty Ltd pays \$15,000 infringement notice penalty* (31 January 2014).

- (c) [REDACTED]

- (d) [REDACTED]

- (e) [REDACTED]

- (f) D2MX Pty Ltd paid a total penalty of \$110,000 to comply with an infringement notice given to it by the MDP. The penalty was for:
- (i) failing to ensure that its AOP system had in place organisational and technical resources, including a 'price movement from last' automated filter and processes to record any changes to the automated filters (which interfered with the efficiency and integrity of the ASX market and the proper functioning of the trading platform); and
 - (ii) failing to prevent the entry into the trading platform of an erroneous order which resulted in a market for BHP Billiton Limited exchange traded March 2012 \$43.51 put options not being both fair and orderly.

See Media Release ([14-095MR](#)) *D2MX Pty Ltd pays \$110,000 infringement notice penalty* (6 May 2014).

- (g) Merrill Lynch Equities (Australia) Limited paid a penalty of \$65,000 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 a market for RIO Tinto Limited ordinary shares not being both fair and orderly: see Media

Release ([14-123MR](#)) *Merrill Lynch Equities (Australia) Limited pays \$65,000 infringement notice penalty* (10 June 2014).

- (h) Credit Suisse AG paid a penalty of \$88,400 to comply with an infringement notice given to it by the MDP. The penalty was for:
 - (i) offering and allocating an error trade to a client in circumstances where that trade had not been obtained under instructions previously obtained from that client;
 - (ii) acting in a manner that had a detrimental effect on that client's best interests; and
 - (iii) failing to maintain a separate record of that error trade.

See Media Release ([14-188MR](#)) *Credit Suisse AG pays \$88,400 infringement notice penalty* (4 August 2014).

102 Pursuant to reg 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 at www.asic.gov.au/infringement-notices.

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
14-009MR	Citigroup Global Markets Australia Pty Limited pays \$40,000 infringement notice penalty	21 January 2014
14-014MR	ASIC accepts enforceable undertaking from BNP Paribas	28 January 2014
14-019MR	Pershing Securities Australia Pty Ltd pays \$15,000 infringement notice penalty	31 January 2014
14-025MR	Diploma Group Ltd issued infringement notice for continuous disclosure breach	10 February 2014
14-049MR	Commonwealth Securities Limited pays \$55,000 infringement notice penalty	17 March 2014
14-050MR	Instinet Australia Pty Limited pays \$50,000 infringement notice penalty	17 March 2014
14-054MR	Hartleys Limited pays \$35,000 infringement notice penalty	19 March 2014
14-063MR	Three Sydney men convicted of insider trading	1 April 2014
14-095MR	D2MX Pty Ltd pays \$110,000 infringement notice penalty	6 May 2014
14-100MR	Two men arrested for insider trading and abuse of public office, \$7 million restrained	9 May 2014
14-123MR	Merrill Lynch Equities (Australia) Limited pays \$65,000 infringement notice penalty	10 June 2014
14-131MR	New South Wales man jailed for market manipulation	17 June 2014
14-133MR	Newcrest admits to breaching continuous disclosure laws	18 June 2014
14-188MR	Credit Suisse AG pays \$88,400 infringement notice penalty	4 August 2014

Key terms

Term	Meaning in this document
ADA	Accredited derivatives adviser
AFP	Australian Federal Police
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
ASIC Market Integrity Rules (Competition in Exchange Markets) 2011	Rules made by ASIC under s798G of the Corporations Act that are common to markets dealing in equity market products quote 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

Term	Meaning in this document
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
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

Term	Meaning in this document
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).
Product Disclosure Statement (PDS)	<p>A document that must be given to a retail client in relation to the offer or issue of a financial product in accordance with Div 2 of Pt 7.9 of the Corporations Act</p> <p>Note: See s761A of the Corporations Act for the exact definition.</p>
Rule 5.6.1 (ASX) (for example)	A rule of the ASIC Market Integrity Rules (ASX Market) 2010 (in this example numbered 5.6.1)
securities dealer	An AFS licensee who is not a market participant but sells securities products through a market participant
Statement of Advice (SOA)	<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	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