Commonwealth of Australia Gazette
MDP01/21, Tuesday, 18 May 2021 Published by ASIC

ASIC Gazette

Contents

Markets Disciplinary Panel: Infringement Notice

Recipient: Macquarie Securities Australia Limited

The recipient has complied with the infringement notice. Compliance is not an admission of guilt or liability; and the recipient is not taken to have contravened subsection 798H(1) of the *Corporations Act 2001*.

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

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PART 7.2A OF THE CORPORATIONS REGULATIONS 2001

INFRINGEMENT NOTICE

To: Macquarie Securities Australia Limited ACN 002 832 126

Matter: MDP 1120/20

Date given: 19 April 2021

TAKE NOTICE: The Australian Securities and Investments Commission ("ASIC") gives this infringement notice to Macquarie Securities Australia Limited (MSAL) under regulation 7.2A.04 of the Corporations Regulations 2001 ("the Regulations"), which is made for the purposes of section 798K of the *Corporations Act 2001* ("the Act").

To comply with this notice MSAL must pay a penalty to ASIC, on behalf of the Commonwealth, in the sum of **$126,000**. This penalty amount represents 600 penalty units, where the amount of a penalty unit is $210.

Unless a contrary intention appears, capitalised terms used in this notice have the same meaning as in Rule 1.4.3. of the *ASIC Market Integrity Rules (Securities Markets) 2017* ("the Rules") as in force at the time of the conduct.

Background

1. In February 2019, MSAL was engaged by an ASX-listed company to act as the broker to conduct, on behalf of the company, an on-market buy-back.

2. MSAL conducted the buy-back across three financial markets, namely:

   (a) the "lit" market operated by ASX Limited;

   (b) the "lit" market operated by Chi- X Australia Pty Limited; and

   (c) relevantly in this matter, the "dark" market being ASX Centre Point (ASXC), operated by ASX Limited.

3. ASXC is open to all market participants. Participants may enter Bids and Asks into the Order Book for that "dark" market but such Bids and Asks are not visible to the rest of the market before the orders are matched as trades.

4. The ASX also offers participants an option of participant preferencing functionality in ASXC. Where a participant enables this functionality, the participant's orders will be

satisfied before any existing unmatched orders submitted by other participants, unless those unmatched orders have price priority.

5. A "buy-back" by a company means the acquisition by the company of shares in itself: section 9 of the Act. An "on-market buy-back" means a buy-back by a listed corporation on a prescribed financial market in the ordinary course of trading on the market: see section 9 of the Act. Regulation 1.0.02A of the Regulations specifies that ASX Limited, among others, is a "prescribed financial market".

6. Neither the Act nor the Rules define the meaning of the phrase "ordinary course of trading". *ASIC Regulatory Guide 110: Share buy-backs* at RG 110.61 states:

> In Australia, this phrase means that the trading is in strict order of price and time priority, with indifference as to the identity of counterparties, and no pre-arrangements or selection of counterparties: see *Attorney-General (Vic) v Walsh's Holdings Ltd* [1973] VR 137.

7. The Markets Disciplinary Panel ("the MDP") considers that orders that are matched otherwise than in price / time priority are not in the *ordinary* course of trading.

Obligation to act in accordance with client instructions

8. Rule 3.3.1(b) of the Rules relevantly provided:

> A Market Participant must not: …
>
> (b) enter into a Market Transaction for a Client, except in accordance with the instructions of the Client, or of a person authorised in writing by a Client to give such instructions …

9. The MDP is satisfied that the client gave instructions to MSAL to conduct an on-market buy-back on behalf of the client, which included an overarching instruction for it to be conducted in the *ordinary* course of trading on a prescribed financial market. The client did not give any instruction to MSAL which expressly prohibited MSAL from submitting Bids under the buy-back on ASXC.

10. The MDP notes that since 10 September 2013, participant preferencing had been activated for all of MSAL's transactions executed on ASXC, without exception. Participant preferencing cannot be activated on a transaction-by-transaction basis or in respect of transactions for a specific client.

11. A total of 3 Bids, which resulted in 6 buy-back transactions, on ASXC are the subject of consideration in this matter, namely:

    (a) 27 March 2019: MSAL entered Client Bid 1 (3 million shares at a price of "MKT") and 34 seconds later entered Client Ask 1 (2.95 million shares at a price of "MKT–0.5"), which resulted in a transaction of 2.95 million shares at a price of $2.495;

    (b) 28 March 2019: MSAL entered Client Bid 2 (525,000 shares at a price of "MKT") and 21 seconds later entered Client Ask 2 (500,000 shares at a price of "MKT–0.5"), which resulted in a transaction of 500,000 shares at a price of $2.405;

(c) 6 May 2019: MSAL entered Client Ask 3 (1.2 million shares at a price of "MKT–0.5") and, immediately after, MSAL entered Client Bid 3 (4 million shares at a price of "MKT"), which traded against Client Ask 3, resulting in a transaction of 1.2 million shares at $2.465. This trade occurred *before* two other trades resulting from matching with Client Bid 3. These two other trades related to two Asks of another participant that had time priority over Client Ask 3. These other two transactions were for significantly smaller volumes, being 742 shares and 459 shares both at $2.465.

(d) 6 May 2019: After Client Bid 3 was entered, MSAL entered 3 further Asks:

(i) MSAL Client Ask 4 (1.2 million shares at a price of "MKT–0.5") was entered 13 milliseconds after Client Bid 3, which traded against the residual of that Bid, resulting in a transaction of 1.2 million shares at $2.465;

(ii) MSAL Client Ask 5 (1.2 million shares at a price of "MKT–0.5") was entered 26 milliseconds after Client Bid 3, which traded against the residual of that Bid, resulting in a further transaction of 1.2 million shares at $2.465; and

(iii) MSAL Client Ask 6 (400,000 shares at a price of "MKT–0.5") was entered 38 milliseconds after Client Bid 3, which traded against the residual of that Bid, resulting in a transaction of 398,347 shares at $2.465.

12. The MDP considers that the use by a participant of ASXC as the venue for submitting Bids which result in purchases under an on-market buy-back does not of itself compel a conclusion that the buy-back was not conducted in the ordinary course of trading. Similarly, the use of participant preferencing on ASXC by a participant does not of itself compel such a conclusion because the relevant question is whether it actually conferred a preference on the participant for a particular order or transaction.

13. Having as agent accepted the client's instructions to conduct an on-market buyback for it, MSAL was obliged to ensure it executed orders as directed by the client in the ordinary course of trading. The use by MSAL of ASXC with participant preferencing activated to execute buy-back orders of its client without intervening measures was accordingly very likely to lead to the execution of orders other than in the ordinary course of trading.

14. Intervening measures adopted by MSAL to avoid such circumstances were employed in relation to Client Bids 1 and 2 but due to a technical issue with the algorithm being used by MSAL, the intervening measures failed in relation to Client Bid 3. Client Ask 3 was preferenced ahead of two existing Asks on ASXC that were submitted by another participant and which had time priority.

15. The MDP is satisfied that the purchase of 1.2 million shares at $2.465 resulting from the matching of Client Ask 3 and Client Bid 3 on ASXC on 6 May 2019 was not in the ordinary course of trading. On that basis, the MDP has reasonable grounds to believe that MSAL contravened Rule 3.3.1(b) of the Rules because that transaction was entered into on behalf of MSAL's client other than in accordance with the

instructions of the client.

16. With respect to the other 5 transactions set out in paragraph 11 of this notice, the MDP is not satisfied those transactions were not in the ordinary course of trading. Although participant preferencing on ASXC was activated at the time these transactions occurred, the transactions occurred in accordance with price / time priority.

Fair and orderly market for a financial product

17. Rule 5.9.1 of the Rules relevantly provided:

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

18. The MDP considers that a buy-back transaction that is not in the ordinary course of trading has the potential to have also created an unfair or disorderly market for a financial product. However, it does not necessarily follow that it has produced that result.

19. The MDP considers that an assessment of whether a participant's conduct has resulted in a market for a financial product not being both fair and orderly primarily involves a consideration of the effect (if any) of the conduct on the price of the financial product and the effect (if any) on the ability of others to participate in the orders and transactions.

20. The MDP is not satisfied that MSAL's conduct resulted in the market for the shares not being both fair and orderly in respect of any of the 3 Bids, which resulted in 6 buy-back transactions. Even in relation to the transaction which resulted from the matching of Client Ask 3 and Client Bid 3 and which was not in the ordinary course of trading, the MDP is not satisfied that MSAL's conduct affected the price of the shares or resulted in the other participant's existing Asks not being able to transact with Client Bid 3. The other participant's existing Asks did trade with Client Bid 3.

The determination of penalty

21. In determining the appropriate penalty, the MDP considered the four key factors set out in *ASIC Regulatory Guide 216: Markets Disciplinary Panel*, namely:

    (a) the character of the conduct;

    (b) the consequences of the conduct;

    (c) the participant's compliance culture;

    (d) remedial steps taken by the participant.

22. MSAL's transmission of the buy-back orders through ASXC was careless because MSAL failed to ensure price / time priority for the buy-back orders. In particular:

    (a) that MSAL adopted an algorithm as an intervening measure when conducting

part of the on-market buy-back on ASXC indicated that it rightly harboured doubts as to whether the use of participant preferencing on ASXC without such an intervening measure would result in trades that were in the ordinary course of trading;

(b) MSAL artificially managed the increase in the Bid volume, aware of the imminent Ask volume of its institutional clients yet to be entered, letting the Bids rest for a short arbitrary period in the dark (but common) pool of ASXC.

(c) MSAL adopted a compliance protocol in an attempt to avoid contraventions, but was alert to the risks it took in adopting the process if the protocol did not operate as MSAL intended. While the conduct resulted in a single contravention of the rules, it was not the sole order that MSAL managed in this manner.

23. The transaction on 6 May 2019 was effected at the mid-point of the market and did not affect the price of the shares or result in the other participant's existing Asks not being able to transact with Client Bid 3. Nonetheless, MSAL created a situation where the issuer may have acquired its own shares in a manner not permitted by the Act.

24. MSAL had made an inquiry of ASIC in April 2015 in relation to the use of ASXC with participant preferencing, and had formulated its policies and protocols in light of ASIC's response. This approach is suggestive of a market participant endeavouring to comply with its obligations.

25. MSAL's recent disciplinary history before the MDP is not unblemished. MSAL has been sanctioned by the MDP on four occasions over the last 6 years in relation to alleged contraventions of the market integrity rules, resulting in the giving of infringement notices in 2015 ($110,000), 2016 ($120,000), 2017 ($505,000) and 2019 ($300,000). However, none of these previous disciplinary matters related to on-market buy-backs on lit or dark markets.

26. The MDP also notes that MSAL chose to take subsequent remedial steps to ensure that no buy-back trading would be routed through ASXC. MSAL has not used ASXC to effect buy-back trading since 25 November 2020.

27. The MDP has sanctioned both UBS Securities Australia Ltd (MDP 02/18: penalty $120,000) and Credit Suisse Equities (Australia) Ltd (MDP 01/20: penalty $75,000) for their respective conduct in relation to on-market buy-backs. Those matters concerned "trades with price improvement" which the MDP considered were not in the ordinary course of trading. In the UBS matter, the conduct concerned six on-market buy-backs over a period of six months. In the Credit Suisse matter, the conduct concerned three on-market buy-backs over a period of eight months. In contrast to the UBS and Credit Suisse matters, the MDP has found a single contravening transaction for a single buy-back client on a single day in relation to MSAL.

28. ASIC Regulatory Guide 216 states at paragraph RG 216.102 that the amount of the penalties specified in infringement notices in relation to conduct occurring before 13 March 2019 will be of limited precedent value in determining the appropriate

penalties specified in infringement notices in relation to comparable conduct occurring on or after 13 March 2019. The penalties specified in the UBS and Credit Suisse matters were based on the previous penalties regime and are of limited precedent value.

29. The circumstances of the MSAL matter are such that the penalty should be at the lower end of the low range. The maximum penalty for a single contravention is 15,000 penalty units. The low range would be up to 5,000 penalty units. A penalty of 600 penalty units represents 12% of 5,000 penalty units, which reflects a penalty at the lower end of the low range.

30. The material uplift in the penalty is in recognition that the increased maximum penalty under the new penalties regime warrants an increase in the level of penalties from those imposed in prior MDP determinations, even at the lower end of the low range.

Other observations by the MDP

31. Although the enabling of participant preferencing on ASXC by MSAL only resulted in a preference on MSAL in relation to one of the orders under consideration and, even then, did not ultimately result in the orders of the other participant not being filled by the existing Bid, that was attributable to fortuitous circumstance rather than by design.

32. Given the increased risk that participant preferencing will likely result in transactions not being in the ordinary course of trading, the MDP guides participants to consider whether on-market buy-backs should conducted through ASXC, where participant preferencing is enabled. This may also be a question of policy for ASIC and the market operators.

Other information

The maximum pecuniary penalty payable under an infringement notice in relation to an alleged contravention of subsection 798H(1) of the Act, by reason of contravening Rule 3.3.1(b) of the Rules, is $3.15 million.

Note: The maximum pecuniary penalty is 15,000 penalty units for a body corporate: see subsection 798K(2) of the Act. The amount of a penalty unit as at the time of the conduct to which this infringement notice relates was $210: see subsection 4AA(1) of the *Crimes Act 1914* (Cth).

The maximum pecuniary penalty that a Court could order MSAL to pay for contravening subsection 798H(1) of the Act (a civil penalty provision), by reason of contravening Rule 3.3.1(b) of the Rules, is determined by section 1317G of the Act.

Note: Under subsections 1317G(2) and (4), the maximum pecuniary penalty is the greatest of:

(a) 50,000 penalty units; and

(b) if the Court can determine the benefit derived and detriment avoided because of the contravention—that amount multiplied by 3; and

(c) either:

(i) 10% of the annual turnover of the body corporate for the 12-month period ending at the end of the month in which the body corporate contravened, or began to contravene, the civil penalty provision; or

(ii) if the amount worked out under subparagraph (i) is greater than an amount equal to 2.5 million penalty units—2.5 million penalty units.

To comply with this infringement notice, MSAL must pay the penalty within the compliance period. The compliance period starts on the day on which this notice is given to MSAL and ends 27 days after the day on which it is given. This penalty can be paid using the method detailed in the email by which this notice is given.

The effects of compliance with this infringement notice are:

(a) any liability of MSAL to the Commonwealth for the alleged contravention of subsection 798H(1) of the Act is discharged; and

(b) no civil or criminal proceedings may be brought or continued by the Commonwealth against MSAL 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; and

(c) no administrative action may be taken by ASIC under sections 914A, 915B, 915C or 920A of the Act against MSAL 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; and

(d) MSAL is not taken to have admitted guilt or liability in relation to the alleged contraventions; and

(e) MSAL is not taken to have contravened subsection 798H(1) of the Act.

MSAL may choose not to comply with this infringement notice, but if MSAL does not comply, civil proceedings may be brought against it in relation to the alleged contravention.

MSAL may apply to ASIC for withdrawal of this infringement notice under regulation 7.2A.11 of the Regulations and for an extension of time to comply under regulation 7.2A.09 of the Regulations.

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

Grant Moodie
Counsel to the Markets Disciplinary Panel
with the authority of a Division of the Australian Securities and Investments Commission

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.