

# INVESTIGATING AND PROSECUTING MARKET MANIPULATION



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## I. INTRODUCTION

Public confidence in the fairness of markets enhances their liquidity and efficiency. Market manipulation harms the integrity of, and thereby undermines public confidence in, securities and derivatives markets by distorting prices, harming the hedging functions of these markets, and creating an artificial appearance of market activity. Accordingly, authorities around the world need to have adequate systems in place to detect, investigate and prosecute market manipulation<sup>2</sup>.

While the character and harmful market effects of market manipulation are well known, the incentives, means and opportunities for carrying out manipulative schemes continue to evolve. As new products and new technologies are developed, as new market participants undertake trading activity, and as trading on global and interconnected markets continues to grow, the risk of cross-border and cross-market manipulation increases.

Furthermore, with the growth of derivative products, there may be an increased incentive to manipulate the asset underlying the contract. For example, the price of securities can be manipulated to affect the price of a derivative contract or other products (e.g., convertible preferred shares) that are tied in some form to those securities. When such distortions occur, innocent counterparties and market participants who engage in transactions at those manipulated prices can be harmed, including public companies, pension funds, collective investment vehicles, banks, and governmental bodies.

The Internet also has increased the opportunities for manipulating the market for securities. With its development as a popular tool for exchanging information about securities, the Internet has become an easy and inexpensive method to disseminate information to vast numbers of people instantaneously. The Internet thus also provides

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<sup>1</sup> This report undertakes to provide information on manipulation that takes into account enforcement issues raised by cross-border and cross-market conduct. Work on this report was undertaken following substantial work in this area at the Tokyo Conference of Commodity Futures Market Regulators which issued guidance on Standards of Best Practice for the Design and/or Review of Commodity Contracts and on Components of Market Surveillance and Information Sharing. See *also* the Report of the IOSCO Technical Committee on the Application of the Tokyo Communiqué to Exchange Traded Financial Derivatives Contracts, dated September 1998.

<sup>2</sup> This report is intended to be descriptive in nature and is not intended to prescribe the specific contours of manipulative conduct that are or should be prohibited in the jurisdictions of the members of the Technical Committee Working Group on Enforcement and the Exchange of Information (TCWG-4). It should be noted that this report does not address legally permissible practices, which may have an effect on market prices. For example, price stabilization efforts are permitted in some jurisdictions.

an unparalleled opportunity to disseminate information about a particular security with the intention of moving its price or even creating the appearance of an active market in a security.

The existence of global and interconnected markets increases the opportunities for market manipulation, as well as the difficulty in detecting and investigating manipulation. The securities, derivatives and the underlying assets whose prices are manipulated may be traded on one market or in one jurisdiction while the persons responsible for the manipulation may be located elsewhere. Indeed, the price of securities or derivatives may be manipulated in one market for the express purpose of affecting their price, or the price of underlying assets, in another jurisdiction or market. Where, for example, derivatives traded in one country are based on an underlying foreign securities index, there may be a motive to manipulate the market for the securities comprising the index. As a result, regulators of both markets can be faced with the challenge of obtaining information regarding trading and positions located in the other jurisdiction. In addition, regulators and authorities may need access to information relating to foreign bank accounts. In certain circumstances, the use of foreign nominee corporations complicates the collection of information and the detection of the illegal activity.

It should be noted that, in some jurisdictions, regulators do not have direct powers to investigate market manipulation. Nevertheless, even if not vested with these powers, regulators need to be cognizant of the manipulative conduct that is prohibited in foreign markets, particularly in an era of global markets. Regulators should also be aware of the wide range of methods used for detecting market manipulation. While the specific elements of investigating and proving manipulation may differ in various legal and regulatory systems, regulators of international markets should have a common understanding of the types of information that can be useful in such proceedings. Moreover, regulators should understand the challenges that exist in taking enforcement action against market manipulation. This Report seeks to assist regulators in their efforts to ensure that they have effective systems in place to address manipulative activity.

Finally, regulators need more than ever to work together and with others to prevent market manipulation where possible and to cooperate in its detection, investigation and prosecution. Regulators must often seek assistance both domestically and internationally to obtain relevant information regarding manipulative activities. Therefore, they need to be able to be assured of the assistance of other authorities. Regulators should work in partnership with their domestic exchanges to the extent possible. Where necessary, they should promote and facilitate cooperation between exchanges. In addition, regulators should be able to obtain assistance from their foreign counterparts, either through Memoranda of Understanding, or other formal or informal arrangements. Where appropriate, regulators may also need to obtain cooperation from other authorities who have access to and the ability to share information useful to investigating and proving market manipulation.

Drawing on the practical experiences of the members of the Technical Committee Working Group on Enforcement and the exchange of Information (TCWG-4), this report:

- sets forth the nature of the manipulation violation in the jurisdictions of TCWG-4 members ;
- identifies measures that can be useful and effective in the detection, investigation and prosecution of manipulative activity ;
- explores the role of exchange-to-exchange cooperation (when permitted by law) in detecting and investigating potential manipulations and ascertains the specific vehicles available for cooperation and information sharing between exchanges and between exchanges and regulators ;
- takes note of the circumstances where international cooperation in the investigation and prosecution of manipulative activity may be needed ; and
- recommends that securities and derivatives regulators charged with enforcing laws, regulations and rules that prohibit manipulative conduct should have :
  - effective tools to prevent and detect market manipulation, including laws that proscribe manipulation with sufficient clarity and flexibility to allow prosecution of novel manipulative schemes ;
  - adequate authority to investigate, prosecute, and deter market manipulation and/or the ability to work with other domestic authorities that investigate, prosecute and deter market manipulation ; and
  - the ability to cooperate at all stages of a matter -- from surveillance, through investigation, to commencement of an action -- across markets and across borders.

This report recognizes that the possibility of manipulation is, in part, a function of the characteristics (e.g. size and liquidity) of the market and, in the case of derivatives, the underlying cash market as well. Jurisdictions have different approaches to defining, detecting, investigating and prosecuting market manipulation and this report is not intended to recommend one specific approach over another. Rather, it can serve as a practical resource concerning the various regulatory approaches taken with regard to manipulation. The drafters are aware that confidence in the fairness of markets enhances their liquidity and efficiency, and that regulation should seek to bolster such confidence by effectively detecting, investigating and prosecuting manipulation. However, the working party also recognizes that regulation should not unduly restrict the freedom to trade.

## **II. TYPES OF MANIPULATIVE CONDUCT**

The elements that comprise manipulative conduct tend to vary depending on the type of market<sup>3</sup>. The sanctions applicable for violations of laws and rules prohibiting market manipulation also vary from jurisdiction to jurisdiction. In some jurisdictions, manipulative conduct is a criminal offense and can result in criminal liability only. In other jurisdictions, manipulative conduct can lead to civil/administrative liability or both criminal and civil/administrative liability. Moreover, in some jurisdictions, manipulation of the securities market is addressed differently from manipulation of the derivatives market. It is also the case that some authorities choose not to define specific violative conduct in a statute or rule; rather, they define the contours of the illegal conduct through case law or other precedent. What follows below is a discussion of some of the elements that comprise the manipulation offense as well as some examples of manipulative conduct.

Types of manipulative conduct may be categorized according to the methods used, the objectives of the underlying activity, and the parties involved<sup>4</sup>.

### **A. Methods**

A number of the methods used include:

- Engaging in a series of transactions that are reported on a public display facility to give the impression of activity or price movement in a security (*painting the tape*)<sup>5</sup> ;
- Improper transactions in which there is no genuine change in actual ownership of the security or derivative contract (*wash sales*) ;
- Transactions where both buy and sell orders are entered at the same time, with the same price and quantity by different but colluding parties (*improper matched orders*) ;
- Increasing the bid for a security or derivative to increase its price (*advancing the bid*) ;

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<sup>3</sup> Members of TCWG-4 submitted short papers describing the manipulation laws in their jurisdictions. These submissions helped to identify the authorities within each jurisdiction with responsibility for addressing such offenses and the scope and source of their enforcement powers. A summary of these submissions is contained in Annex 1. Certain members of the Emerging Markets Committee Working Group on Enforcement and Exchange of Information (EMCWG-4) also provided information on the manipulation laws in their jurisdictions. A summary of these submissions is contained in Annex 3.

<sup>4</sup> Examples of certain types of manipulative conduct have been provided by members of TCWG-4, based on manipulation cases from their respective jurisdictions. Most of the examples involve transactions or other activities carried out in more than one market. These examples are described in Annex 2 to this report.

<sup>5</sup> Wash sales and improper matched orders are often used in manipulations involving painting the tape.

- Buying activity at increasingly higher prices. Securities are sold in the market (often to retail customers) at the higher prices (*pumping and dumping*) ;
- Buying or selling securities or derivatives contracts at the close of the market in an effort to alter the closing price of the security or derivatives contract (*marking the close*) ;
- Securing such control of the bid or demand-side of both the derivative and the underlying asset that leads to a dominant position. This position can be exploited to manipulate the price of the derivative and/or the asset (*corner*). As regards derivatives, in a corner, a market participant or group of participants accumulates a controlling position in an asset in the cash, derivative and other markets. The market participant or group of participants then requires those holding short positions to settle their obligations under the terms of their contracts, either by making delivery or by purchasing the asset from the manipulator or by offsetting in the derivatives market opposite the manipulator at prices distorted by the manipulator ;
- Taking advantage of a shortage in an asset by controlling the demand-side and exploiting market congestion during such shortages in such a way as to create artificial prices (*squeeze*) ; and
- Dissemination of false or misleading market information through media, including the Internet, or by any other means. The dissemination is done in order to move the price of a security, a derivative contract or the underlying asset in a direction that is favorable to the position held or a transaction planned by the person disseminating the information<sup>6</sup>.

## **B. Objectives**

The objective of manipulative conduct will normally be to make money either directly through transactions, or by other means. Some examples of how this motive is achieved include:

- Influencing the price or value of a security or a derivative contract, so that the manipulator can :
  - buy at a lower price,
  - sell at a higher price,
  - influence takeover bids, or other large transactions, or
  - combat competitive transactions ;
- Influencing the price of a derivative contract or the underlying asset ;

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<sup>6</sup> In some jurisdictions, dissemination of false or misleading information constitutes a separate offense prosecuted under laws not specifically directed at manipulation.

- Influencing the price of a security underlying an index ;
- Influencing the subscription price in public or non-public offerings ;
- Influencing the price/conversion ratio in connection with merger of companies ;
- Influencing the price of a security in connection with take-over offers ;
- Influencing someone to subscribe for, purchase, or sell assets or rights to assets, or to abstain from doing so ;
- Influencing the accounts/balance sheet of institutional investors ;
- Influencing the limit for triggering forced sale by creditors ; and
- Influencing the impression of financial advice or placements.

### **C. Parties involved**

Those in a position to effect a manipulation include:

- Issuers of securities ;
- Participants in the securities market, derivatives market or underlying cash market ;
- Market intermediaries ; and
- Any combination of the above acting in cooperation with one another.

It is important to note that the methods used in many manipulation cases involve transactions or other activities carried out in two or more affected markets. These markets may be within the same or different jurisdiction. Manipulation involving cross-border activities often involves parties (physical and/or legal persons) that are domiciled in different jurisdictions.

## **III. TOOLS FOR PREVENTING MARKET MANIPULATION**

There is a wide range of tools that are used to prevent and deter manipulative conduct in both securities and derivatives markets. Anti-manipulation regulation focuses on maintaining the integrity of the market price of securities, of derivatives contracts and of

the assets underlying such contracts. The rules attempt to ensure that a price is set by the unimpeded collective judgement of buyers and sellers. In addition, the rules attempt to prevent introduction of misinformation into the market and abuse of market power. Such rules enhance a regulator's ability to secure the independent trading and pricing mechanism of the marketplace<sup>7</sup>.

In some jurisdictions, manipulation may be prosecuted under rules that govern fraudulent activity. As an example, one jurisdiction can prosecute as a fraud, a transaction in a security that either creates actual or apparent trading in such security or causes a rise or decline in the price of such security, and that is intended to defraud or that operates as a fraud or deceit, upon the market for the security.

Rules imposing disclosure requirements should be considered as an additional tool for preventing manipulation. For example, requesting the issuer of listed securities to disclose timely price sensitive information is aimed, among other things, at reducing information asymmetries that can facilitate manipulation. The timely dissemination of trading data (both pre and post-trade) is also crucial to reduce information asymmetries among market participants.

Some jurisdictions may also have rules that prohibit manipulation in specific situations. For example, such rules can prohibit manipulative activities on particular markets. In addition, a jurisdiction can have rules that prohibit manipulation by particular market participants. Some rules require a showing of manipulative intent or purpose. In addition to the broad prohibitions at the core of anti-manipulation rules, there are a number of other provisions and tools designed to prevent manipulation. Some are discussed below.

## **A. Securities Markets**

### **1. Short selling rules**

In certain jurisdictions, a short sale is defined as the sale of a security that the seller does not own or that the seller owns but does not deliver to the purchaser. In order to deliver the security to the purchaser, the short seller will borrow the security, typically from a broker or an institutional investor. The short seller later closes out the position by returning the security to the lender, usually by making a purchase on the open market. Purchases on margin also may be used by manipulators to accelerate a market trend.

In some jurisdictions, short selling rules prevent sellers from engaging in activities that cause or accelerate declines in securities prices, irrespective of the intention of the short seller. In addition, rules requiring the disclosure of short sales (either to the regulator or the market or both) are used by many jurisdictions to deter or prevent manipulative short selling.

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<sup>7</sup> Disclosure and transparency requirements focus on generating and maintaining integrity of the price formation process, and manipulation prohibitions focus on preventing harm to that integrity.



## **2. Rules limiting participation during offerings**

Securities offerings present special opportunities and incentives for market manipulation. Around the time of an offering, manipulative activities can be used to increase offering proceeds by increasing the market price on which the offering will be priced, or stabilizing the market price to avoid a failed offering. Because price integrity is essential during an offering, some jurisdictions have adopted rules to prevent interested parties from creating artificial prices.

Rules limiting market activity during offerings are designed to protect the integrity of the securities trading market as an independent pricing mechanism. The rules focus on potentially manipulative activities by those likely to profit from the offering, such as by governing the activities of underwriters, issuers, selling security holders, and others participating in an offering of securities. Rather than addressing manipulation after the fact, such rules seek to prevent it. Therefore, these rules do not require proof that distribution participants have manipulative intent or purpose.

## **3. Methods for calculation of index**

There are several methods for calculation of an index, including : capitalization-weighting calculation, modified capitalization-weighting, equal-currency-weighting, and modified equal-currency-weighting. In some jurisdictions, the component weightings are reviewed on a quarterly basis and are adjusted if necessary. In addition, intra-quarterly adjustments are made, as necessary, to reflect corporate actions, share issuances and repurchases, and other events of significance. Terms of any weighting calculation methodology must be clearly defined and widely published and consist of objective standards for initial and continued listing. The various methods exist essentially to ensure that the index is sufficiently balanced and diverse to make attempts to manipulate it more difficult.

In addition, requirements relating to the timing of the calculation and announcement of the level of the index can reduce the possibility for manipulation. Without such requirements, the reshuffling of a stock index, for example, can create an opportunity for manipulation.

To ensure that the trading markets for component securities are adequately capitalized and sufficiently liquid, jurisdictions may impose requirements including, minimum capitalization, monthly trading volume, averaging closing prices by volume and relative weightings of component securities. These requirements are designed to minimize the potential for manipulation of the index.

## **B. Derivatives Markets**

### **1. Contract design**

Derivative contracts operate more efficiently and are less susceptible to manipulation, and less likely to disrupt the operation of cash markets, when the terms of the derivative contract accurately reflect the needs of the particular market in the underlying asset. Designing a derivatives contract to conform to the underlying cash market of the asset requires a detailed understanding of the characteristics and operational features of the relevant cash market. Knowledge of the cash market for an asset is critical in assessing the specifications of a derivative contract based upon that asset. Particular attention should be given to the cash pricing and delivery systems as well as historical patterns of production, consumption and supply of the underlying asset.

In the interest of ensuring proper contract design, some jurisdictions have laws and/or rules requiring that exchanges provide rules for delivery at points, grades and locational price-differentials that will tend to prevent or diminish market manipulation, market congestion or the abnormal movement of the asset in commerce. If the rules of an exchange do not fulfil these purposes, the regulator may have the power to require that the rules be changed.

With respect to option contracts, most have standardized terms, such as the nature and amount of the underlying asset, the expiration date, the exercise price, position limits, whether the option is a call or a put, and whether the option is a physical delivery option or a cash settled option.

## **2. Position limits**

In order to enhance market integrity, the design elements may be accompanied by other structural measures related to the trading of the derivatives contract that can facilitate the deterrence of market manipulation. One such measure adopted in some jurisdictions is restriction on the size of positions that can be held by market participants. Position accountability and position limits are intended to inhibit the development of extraordinarily large exposures in relation to long or short positions controlled on the market and/or in relation to the financial exposure of the member to the exchange as a result of customer or proprietary positions.

Spot month position limits might be designed to prevent market participants from attempting to manipulate the price of an asset by, for example, demanding delivery of more of the underlying asset than is economically available. If imposed, exemptions from or adjustments to position limits may be granted for *bona fide* hedging purposes at levels that do not threaten the orderly liquidation of the expiring contract. Limits concerning the size of a position for one asset for future delivery (or an option thereon) that a single market participant may hold in a single contract month, or in all future months combined, can be established by either the regulatory authority or exchange. To be effective, such limits should be applied to individual market participants and to groups of participants trading pursuant to an express or implied agreement or understanding. It should be noted that concerns regarding the possibility of manipulation will not be the same for all assets. Where, for example, a particular market is exceptionally deep and liquid, position limits may not be as important.

## **IV. TOOLS FOR DETECTING MARKET MANIPULATION**

### **A. Market Surveillance**

The goal of surveillance is to spot adverse situations in the markets and to pursue appropriate preventive actions to avoid disruption to the markets. At a minimum, regulators should have access to current events in the markets. Types of surveillance methods include:

#### **1. Filing of ownership and control of companies**

Rules requiring the filing of documentation of corporate ownership and control assist regulators to determine some of those likely to be in a position to effect a market manipulation or who likely stand to gain significantly from a manipulation. In addition, the ability of regulators to obtain ownership information can be useful.

#### **2. Surveillance systems**

Surveillance programs include a reporting system to permit market authorities to assess large positions in light of other market factors, including deliverable supplies in the cash market, market participants' positions in other markets, concentration of positions and ability to make or take delivery, and financial exposures. Reporting systems capture the daily positions and identities of market participants whenever their open positions in a particular derivative exceed a minimum threshold level and permit market authorities to aggregate positions of related persons to facilitate identification of market power.

Surveillance systems, including information obtained through position reporting, could be designed to capture information that allows the following types of analysis:

- a. tracking of changes in price or volume of a particular security or derivatives contract and underlying asset as well as changes in price or volume of related securities or derivatives contracts and underlying asset ;
- b. identifying concentration of ownership and potential collusive or concerted activity by market participants ; and
- c. conducting financial surveillance to identify potentially large market losses or gains incurred by firms trading for their own accounts, or by large market participants who trade through the firm.

Surveillance systems should be designed to keep pace with technological and market evolution. Exchanges can play an important surveillance role.

## **B. Internet and Other Media Surveillance**

Surveillance of information provided to the public should include media (newspapers, television, newsletters and analysts' research reports, etc.)<sup>8</sup>. In addition, on the securities side in particular, the Internet may require specific attention and surveillance skills because of its characteristics, including its ability to reach vast numbers of people instantaneously. The speed with which information disseminated over the Internet can be changed creates challenges for regulators in identifying and preserving evidence.

## **V. INVESTIGATING MARKET MANIPULATION**

### **A. Proving Market Manipulation**

Given the difference in the nature of securities and derivatives markets, proving a manipulation involving these markets may require different types of evidence and analysis. Separately, the laws in different jurisdictions may be distinct as to the elements that comprise the manipulation violation, and issues of proof will vary accordingly. Additionally, exchanges have responsibilities to maintain orderly markets and prevent manipulation with anti-manipulation rules and in some jurisdictions may have the power to investigate and discipline members who violate these rules. The discussion in this section is not intended to catalogue the common elements of market manipulation in *all* jurisdictions. Rather, it is intended to serve as a discussion of certain elements that TCWG-4 members have identified as necessary to prove manipulation in their jurisdictions.

#### **1. Investigating an artificial price or price effect**

##### **a. Securities**

If a security appears to increase suddenly in price or volume of trading, or both, such that manipulative activity is suspected, the investigator should perform some analysis of the market for the security and why the price or volume, or both, may be changing suddenly. The investigator should examine how the securities were introduced and traded in the market. If the security was previously issued and outstanding, as opposed to being a new issue, the investigation may include an analysis of the security's historical price movements.

In examining the price, one question is what the price was when it was at its highest, and whether there is an explanation for that price. If the price collapsed the question is whether it collapsed after insiders sold their securities or as a result of downward manipulative activity. The investigator should review all the publicly available information concerning the security. In addition, the investigator may be able to obtain useful information on the patterns of trading by examining the performance of peer group

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<sup>8</sup> Such information can include both the touting of stock that can have an upward effect on the price of a particular security, or the spreading of false information that can affect the price of a security.

securities, or the securities of similar companies during the relevant period. The investigation should also consider the condition of the market as a whole -- whether it was a bear, bull, or flat market -- and how the security in question performed as compared to the overall market. Also, for the security in question, it is relevant to determine whether, prior to the manipulation period, the security was thinly traded or even inactive, and how volatile it was. The key question is whether there appears to be any logical trading pattern to the security's price and volume, or whether it seems erratic. If it is erratic, the question is whether the pattern coincides with the activities of the promoter, broker, or other participants in the potential manipulation.

The investigation of potential manipulation should focus on what information was made publicly available during the relevant period. An analysis of such information will indicate whether there is a legitimate basis for the price of the security, or of the asset underlying a derivative contract to have risen, such as favorable financial news or other newsworthy events concerning a company or market. If there is an absence of such information, and the price nevertheless rose significantly, that fact may be indicative of manipulative conduct. If there is no apparent basis for the price increase in the publicly filed or published information, the investigator should determine whether the public information is false or misleading.

#### **b. Derivatives**

Price artificiality is the divergence of price from the legitimate forces of supply and demand. In order to establish price artificiality, it is therefore necessary to accumulate evidence that prices did not follow legitimate economic forces. One way to do this is to establish what the level of price or price relationships would have been, or should have been, had the suspected manipulator not illegitimately interfered with the normal process of price formation. In establishing normative levels or price relationships, it is important to identify as many relevant market forces as possible and to ascertain their effect.

In the cash market for commodity assets, for example, one must consider supply factors such as the deliverable supply of a commodity as specified in the derivatives contract; any "seasonality" that may factor in its supply; all relevant production and marketing trends; and owners of deliverable supply. Likewise, one must identify demand factors such as the major users of a commodity; the location of the users relative to the delivery points of the commodity; changes in economic factors affecting the demand; and demand at the delivery points.

On the derivatives side, one must examine all aspects of open contracts, such as the group composition of the market (i.e. market shares of largest traders); who held derivatives positions of a size sufficient to affect prices; and who held large positions on the other side of the market. Finally, one must consider delivery factors such as who

owned or controlled deliverable supplies; who made deliveries; who received deliveries; and what grade of asset was delivered and where it was located<sup>9</sup>.

## **2. Investigating the possible distortion of the laws of supply and demand**

As an early step in the investigation of a possible manipulation of the market for a security, a derivative contract or the underlying asset, it may be useful to determine whether or not the potential manipulator had the ability to influence market price or volume. This ability can stem from: (1) the manipulator's control of the supply of a security, or of the asset underlying a derivative contract, (2) the relative and absolute size of his derivatives positions, or simply from (3) his specific access to the public market, whether it is through the market itself, or through the Internet or some other medium in which he disseminates false information about the security, the derivative contract, or underlying asset.

### **a. Establishing control of the available supply**

In order to determine whether the suspected manipulator has control of the available supply of a security or of the asset underlying a derivative contract, it is necessary to establish the available supply, how much of that supply is publicly traded or deliverable, and whether the security or asset is owned broadly by many different market participants. For example, the less liquid a security, the easier it is for a person to obtain control of supply without having to own a large proportion of the issued capital. The determination of who controls the available supply of a security or other asset may require analyzing the trading records, and taking steps to investigate who is behind the nominee names (where applicable) in which the security, derivative contract, or asset has been held and traded.

Manipulation cases may involve circumstances where the number of shares outstanding may be high or where the deliverable supply is ample, but the suspected manipulator may have designed and carried out transactions for the purpose of limiting the public float or deliverable supply and placing a large portion of the publicly-traded security or of the asset underlying a derivative contract in the hands of a particular entity or small group of entities.

In order to assess whether the suspected manipulator has control of the available supply, the investigator may wish to examine the available data on OTC transactions. OTC transactions may be used either to finance the purchase of the asset concerned

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<sup>9</sup> Other pertinent surveillance questions for derivatives markets are listed in the September 1998 IOSCO Technical Committee report entitled "*The Application of the Tokyo Communiqué to Exchange-Traded Financial Derivatives Contracts.*"

(e.g., through repo transactions), or to carry out the purchase of such assets. It should be noted that in many jurisdictions OTC transactions are not subject to reporting requirements to regulators.

### **(i) Securities**

On the securities side, there are certain types of transactions that manipulators commonly use to gain control of the publicly traded shares of a company. Some of these transactions are described below, but it should be noted that not all of the following transactions, or the statutes and rules that they are designed to evade, are applicable to all jurisdictions.

Manipulators frequently initiate the manipulation by acquiring a dormant public corporation (“shell”) and merging it with a privately-held company. Manipulative schemes that begin with the acquisition of a public shell commonly involve reverse stock splits. The purpose of the reverse stock split is to reduce the number of authorized shares so that the shares can be better controlled by the insiders and there is less likelihood of a significant percentage of outstanding shares ending up in the public float.

Manipulators can also gain control of a public company via the initial public offering (“IPO”). For example, in a “blank check” type of scheme, a promoter/manipulator sells securities to the public, but the use of proceeds and business of a company are not determined prior to the IPO. The promoter and accomplices receive large blocks of control shares for nominal consideration prior to the IPO. The lead market maker for the securities acts in cooperation with the promoter and advances the bid, despite absence of legitimate demand and order flow. The market maker dominates the market through price leadership and control of the float. Through that domination and control of the market, and through the use of materials to promote the security, the market maker and promoter are able to manipulate the price of the security.

A third method for the manipulators to gain control of the issuer or a large block of securities is more straightforward: if the manipulation is being carried out by management of the issuer, or if the manipulator is working closely with management, management may simply cause the company to issue unregistered securities in large quantities to themselves and to their co-conspirators through nominees. In doing so, they typically misuse various exemptions from registration requirements to avoid registering the securities. The exemptions from registration that are commonly abused include: (1) exemptions for securities issued by a company as compensation to advisors and consultants ; (2) exemptions for small offerings, or private placements ; and (3) exemptions for securities sold in a foreign country. After the security’s price has been manipulated to the desired level, management and its nominees can sell their securities at a profit.

The above-described methods of gaining control of the supply of a security are examples only, and are not the exclusive means that may be used to achieve such control even in the jurisdictions to which they apply. The methods described, however, illustrate three techniques to place control of the security into the possession of the manipulators, and may be used in combination with one another.

## **(ii) Derivatives**

In a “corner”, involving derivatives markets, a market participant or group of participants acquires control of the available supply of the asset in the cash market and the derivatives market. The market participant or group of participants then requires those holding short positions to settle their obligations under the terms of their contracts either: by making delivery by purchasing the asset underlying the derivative contract from the manipulator; or by offsetting in the derivatives market opposite the manipulator at artificially high prices dictated by the manipulator. To establish control of the available supply of the asset, an investigator would need to determine the supply of the asset held or controlled by the suspected manipulator as well as the long positions directly or indirectly held by the suspected manipulator on-exchange and in the over-the-counter market.

### **b. Establishing the ability to influence market price without controlling the available supply or demand**

In some cases, the manipulator may not control the supply of a security or of the asset underlying a derivative contract, but may use various other means to manipulate the price, such as disseminating false information about the relevant company or taking advantage of a congested market. False information about the company or the derivative or cash market, which influences the price of the company's shares or of the asset underlying a derivative contract may be disseminated in publicly filed financial statements, press releases, or through some other medium.

The Internet creates special challenges in fighting market manipulation: it is an efficient and quick way to reach large numbers of potential investors, and it is particularly significant in the international realm because it provides a new medium for fraud to be committed more easily across borders. For example, the owners or promoters of a company may set up a Web page with false financial information or false statements about the company's products. They can then use e-mail to contact as many investors as possible, using e-mail addresses that they have collected on the Internet, for the purpose of touting the company. The false information and touting may be spread further by the use of newsgroups and Web discussion sites dedicated to investing. Additionally, the Internet may allow individuals seeking to manipulate the market to act anonymously or to impersonate a legitimate source of information.

It also has become common for publishers of securities newsletters, which offer recommendations on particular securities, to publish their newsletters and recommendations on the Internet. The publishers of such newsletters may have been paid by the issuer or promoter, in the form of securities or monetary compensation, to tout their securities.



Finally, a manipulator who is not affiliated with the issuer can obtain a block of a security and then use Internet investment sites to disseminate false information about the security. He can then monitor the market prices and sell when the security reaches a sufficiently high level.

### **(iii) Securities**

In cases involving either unexplained increases in an issuer's share price, or the dissemination of potentially false financial or business information, the investigator should analyze the issuer's financial statements. Such analysis should include an examination of what assets support the company's security, whether those assets are real, a review of the company's earnings, both past and current, and an analysis of whether the financial statements support the price at which the security is trading.

In addition to analyzing the company's financial statements, the investigation should focus on whether the company has a current or proposed product that would justify the price at which the security is currently trading, or whether, instead, the product is bogus or in a preliminary, untested stage. In cases involving the manipulation of the securities of penny stocks or microcap companies, it is common to exaggerate or even fabricate potential and existing demand for the company's product, and possibly the stage of development of the product.

### **(iv) Derivatives**

In addition to disseminating false or misleading market information, a participant could potentially manipulate the price of a derivative contract or the underlying asset without controlling the available supply by exacerbating market congestion caused by a naturally occurring shortage of the asset. In such a "squeeze," the manipulator has the ability to influence prices by increasing his/her long position in the derivatives market. As the shorts enter the delivery period and realize that they do not hold sufficient supplies of the asset to satisfy the demands of the longs who stand for delivery, the shorts will bid up the price of the derivative contract and/or the asset to the point where it becomes economically viable to divert supplies from normal commercial channels to delivery points. In an effective squeeze, shorts will have to offset at least part of their position in the derivatives market at artificially high prices dictated by the longs.

## **3. Proving intent**

### **a. Nature of intent**

Not all jurisdictions require intent or proof of intent in order to establish manipulative conduct. When intent is a necessary element to prove manipulation, some jurisdictions focus primarily on whether the conduct at issue was done with fraudulent intent or with the intent to mislead. Other jurisdictions require proof of intent to create artificial prices.

### **(i) Fraudulent intent/intent to mislead**

In many jurisdictions, certain manipulative conduct is defined as conduct involving an intent to defraud or create a false impression in the minds of market participants. This is especially (but not exclusively) true of criminal codes that address manipulative conduct.

## **(ii) Intent to cause artificial prices**

Some jurisdictions focus on the intent to cause artificial prices for certain types of manipulative conduct. The intent to cause artificial prices alone, even in the absence of fraud or deceit, may be considered manipulative. Proving the intent to cause artificial prices in the context of derivatives trading may require that a regulatory authority or prosecutor demonstrate that a market participant did not simply exploit the benefits of a legitimately established positions in advantageous market conditions. Where the market participant holding the long position exacerbates market congestion by intentionally decreasing the deliverable supply or increasing his/her long position in the derivatives market, manipulative conduct might be inferred.

### **b. Establishing un-economic behavior – refute legitimate business purposes**

In establishing intent, the regulatory authority or prosecutor might have to refute arguments that activity undertaken by a suspected manipulator actually serves a legitimate economic purpose. Accordingly, the investigation should include a comparison of the trading or quotation activity to the workings of supply and demand -- prices should not be going up if there is no real demand for the security or asset.

In the securities context, the market participant can be asked if there is any economic justification to be provided for the trades. The investigator should examine the number of times the market participant raised the bid during the relevant period, and examine whether that bid was the leading, equivalent, or lower bid compared to other market makers. Also, the investigation should review those records for evidence that the entities responsible for raising the price had any orders to support their bid and ask quotations. For example, if a market maker raises its bid for 20 days in a row, and yet never did a trade during that time, that would be an indicator of market activity without economic substance, and suggestive of manipulative activity.

For trading in securities, the records should be examined for purposes of determining whether there were any trades outside the quotation. Purchasing by a market participant below its own quotation may be suggestive of manipulation, especially when it is raising the bid price at the same time.

The market participant's inventory should also be studied, including the opening and closing inventory figures. If the firm had a policy regarding acceptable inventory levels to be carried overnight in that type of security, the question is whether that policy was followed. Another important question is whether there were orders to support the inventory level that the firm maintained in the manipulated security. If the market participant is carrying more of the manipulated security in inventory than normal or justifiable, he may be seeking to lock up the floating supply of the security in question.

With respect to derivative contracts that allow for delivery of the underlying product, it will be important to consider whether a legitimate purpose can be established for delivery, such as whether the party seeking delivery has fixed price sales obligations to deliver in the cash market.

**c. Showing motive for affecting market price of a security or creating appearance of active trading in a security**

The usual motivation of participants in a market manipulation is to make money on the sale of the securities being manipulated. To establish such motivation, the investigator may demonstrate ownership by the manipulators and their nominees of a large block of a security or an options position, to be sold at an inflated price. In certain jurisdictions, manipulators also may profit during the offering phase, as well as in the secondary market. For example, offering proceeds may be increased by manipulating the market price on which the offering will be priced. Although motive is not always a necessary element of the manipulation offense on the derivatives side, the manipulator may have a large derivatives or cash position that would benefit from a price movement.

Another possible motivation is the existence of a relationship between entities that may be cooperating with one another from one deal to the next. For example, one broker may be motivated to help with a scheme to manipulate in order to obtain the other broker's cooperation in a future manipulation.

Another possible motivation is the desire to inflate the value of the assets in a portfolio or fund. This goal may motivate fund managers to participate in a manipulation.

Finally, in some manipulative schemes, the issuer, promoter, or other insiders may be paying bribes to the brokers who are carrying out the manipulative trading. In boiler room operations, the broker may be using some of that money to hire relatively new, inexperienced, or unsupervised brokers to make cold calls on potential customers using high pressure sales techniques and using sales scripts.

**B. Maintaining and Collecting Information Necessary to Prove Manipulation**

**1. Record-keeping requirements/reports from self-regulatory organizations, exchanges and intermediaries**

The investigating authority should take advantage of the record-keeping requirements that exist in the relevant jurisdiction. Depending on the circumstances, such as the type of scheme and the parties involved, and the market and trading mechanisms involved, the following types of records should be considered: trading records concerning transactions relating to the security, derivative and/or asset the price of which is being manipulated, including but not necessarily limited to order tickets, confirmations, monthly account statements, trading books, canceled checks, wire transfers, financial instrument ownership transfers, stock transfers, and any other related documents. In addition, data can be obtained from clearing organizations and central depositories. The

identity of account holders and beneficial owners of the securities and derivatives positions is important, in order to identify the customers on whose behalf the trading is being done. It may also be important to obtain the telephone records of the account holders and beneficial owners of the securities or derivatives and any taped telephone conversations between intermediaries and their clients.

The investigator may also need to obtain the trading and telephone records of others who are potentially involved in the manipulation, such as the promoter, the issuer and its management, purchasers, transfer agents, investors, other brokers, and anyone else who may be involved in the scheme. In a case involving the Internet, the investigator may need to seek the information from an Internet service provider or other sources concerning e-mail senders and recipients as well as authors of Web pages.

Another important source of documentation concerning the suspected manipulative trading is the records and audit trails of stock exchanges and, when applicable, self-regulatory organizations. For example, the following types of reports and analyses (among others) may be available, or may be generated from trading data: (1) market maker price movement reports, which may show quotation advances, wide spreads, marking the close, one market maker leading other market makers, and frequent closing quotes; (2) high bid and low offer analysis, which shows the percentage of time a broker firm held the exclusive and shared high bid or low offer among all market makers in the security; (3) reports showing total reported volume and the volume reported by each market maker, on a daily, weekly, or quarterly basis; (4) reports that compare every trade effected in order to determine whether the trade was executed within the inside quote (*i.e.*, highest bid, lowest offer); (5) security watch reports, which will show activity in the market that has caught the attention of the self-regulatory organization or exchange that generated the reports; and (6) marking the close alerts, which will show if a security's closing price has traded outside certain parameters on a frequent basis within a particular time period.

As regards derivatives exchanges, the following types of information may be available, collected or derived from trading data: (1) pricing of contracts throughout the trading day in real-time; (2) transactional information including date of trade, commodity contract, delivery month, expiry date, buy/sell, quantity, counterparties to the contract and price of the contract; (3) positions held by market members (both "whole firm" and individual participants) and market users where the size of the position is above a specified level; (4) the identity of each position holder (by name or code) down to first customer level and the size of the position, by contract month, for each position holder; (5) warehouse stocks or other deliverable supply; (6) OTC transactional information including date of transaction, interest, duration and maturity of contract, buy/sell, quantity, counterparties to the contract and price of the contract; (7) OTC position information; and (8) delivery intentions.

## **2. Bank records**

It may be important to obtain bank records of the various entities and persons involved in the trading of a security, of a derivative contract or of the asset underlying the derivative contract. Such records may reveal or suggest the existence of payoffs, bribes,

the splitting of profits or mutual financing arrangements. The bank records also are likely to be necessary in order to trace the proceeds of the manipulation and eventually obtain a forfeiture or freeze of the assets.

### **3. Telephone records**

The telephone, facsimile, and e-mail records of brokers, customers, investors, insiders in a company, and/or the promoter may reveal information about collusive trading or other manipulative activities.

### **4. Use of regulatory powers to collect information**

The investigating authority may use its various regulatory powers to obtain the types of information discussed above. The various information-gathering powers of the securities or derivatives regulator, or reporting requirements applicable to regulated entities and market participants, may include the following: (a) mandatory position reporting; (b) power to inspect records of registrants and licensees; and (c) power to require hearings or the production of testimony and records from investors, customers, and third parties such as banks and telephone companies.

## **VI. THE CHALLENGES IN TAKING ENFORCEMENT ACTION AGAINST MANIPULATION**

### **A. Standards of Proof**

In many jurisdictions, there is a different standard of proof for civil, administrative, and criminal actions, with the highest standard of proof required for criminal proceedings. In all three types of cases, it will often be difficult for the regulatory authority or prosecutor to obtain direct evidence -- either through documents or testimony -- of manipulation. In some cases, the regulatory authority or prosecutor may be able to obtain such direct evidence, such as the testimony of a co-conspirator that he/she and the defendant intended to manipulate the price of a certain security, derivatives contract or asset underlying the contract.

More commonly, however, the manipulation case will have to be based upon circumstantial or indirect evidence and inferences based upon that evidence. Such inferences may be based on patterns of conduct, the fact that a defendant has a pecuniary interest in a given security, derivatives contract or underlying asset, the defendant's having taken steps to effect a rise in its price and the trading patterns or irregularities that emerge from an analysis of the trading data.

### **B. Reconstructing Trading in the Market**

Trading reports and audit trails from exchanges are good starting points for the reconstruction of trading, from which significant patterns may emerge. Some of the types of analyses and reports available from exchanges and self-regulatory organizations are listed in Section V.B.1. These documents will provide evidence of who was in the market, what possible conditions might have contributed to price movements, and the timing and patterns of the price and volume movements in relation to other occurrences and influences (such as corporate developments, commodity statistics issued by a governmental authority and public announcements of the issuer).

It is important for audit trails to capture the whole course of market trading including timing and sequencing of transactions from the time of order receipt through execution, confirmation and clearing.

In addition, in connection with a potential manipulation of the price of a security, the regulatory authority or prosecutor may want to obtain, and may rely on, offering circulars, prospectuses, disclosure documents, and various other public filings. In addition to publicly filed documents, the proof of manipulation may also include promotional literature and press releases.

### **C. Voluminous Data Management and Analysis**

If all of the relevant trading records are obtained, as well as bank records, corporate documents, and other records, the volume of data and documents may become significant. As a method of organizing the evidence, and in order to demonstrate the likely manipulation, it may be useful to prepare charts showing price and volume history for the applicable period for the relevant security, derivatives contract or underlying asset, or to obtain such charts from commercial market data collection organizations. In addition, when the manipulation case is based on trading, the regulatory agency or prosecutor will need to prepare, when the data are available, a chart of transactions reconstructing the market showing counterparty, price, moving inventory of the market participant, and profits or losses to the trading account on long sales and purchases and on short sales. In addition to charts, investigators may consider using statistical analysis to demonstrate the existence of intention and to refute a claim that the trading was for legitimate business purposes. Both in-house and independent consultants and experts (including academics) can help to organize and analyze the data.

### **D. Use of Expert Testimony**

Expert testimony, either delivered by outside experts or by experts from within the relevant securities or derivatives authority, may be useful to explain to the trier of fact what the patterns of trading are and why they are indicative of manipulation. Also, depending on the rules of the particular jurisdiction, the expert may be used as a shortcut way of getting the trading data into evidence or before the trier of fact as material relied on by the expert in reaching his opinion.

Experts with actual and current experience from the marketplace can assist investigators both during investigations and prosecutions by providing explanations of

what would be considered “normal” market behavior or “legitimate” business activity. Such expertise can assist the investigator in closing investigations that are not warranted and in identifying evidence useful to refute defenses asserted during prosecution.

Depending on the procedural rules of the jurisdiction, there may be limitations on how far the expert witness will be permitted to go in drawing conclusions as to whether there was a manipulation based on the trading patterns and other facts.

## **VII. COOPERATION**

There are many instances in which a regulator must seek assistance, whether domestically or internationally, to obtain relevant information regarding market manipulation. For example, information on manipulative activities may be in the possession of or may only be obtained by another regulator or authority. Also, multiple regulators and authorities can prosecute the same manipulative activity, and sharing information is an efficient use of resources. Therefore, cooperation among regulators and authorities can be useful and may be necessary in detecting suspicious market activity and in investigating and prosecuting market manipulation.

Cooperation exists on different levels. In particular, information sharing takes place between exchanges; between regulators; between a regulator and an exchange; and between a regulator and other types of authorities. Forms of cooperation include sharing information already in one’s possession in response to a request, compelling an individual or entity to produce information (e.g., documents or statement) in response to a request, and proactively providing information to a relevant party.

### **A. Domestic Cooperation**

Cooperation can take place on a domestic level where, for example, an authority other than the regulator (e.g., exchanges) shares responsibility for market surveillance. Cooperation also can take place where an authority other than the regulator has the ability to obtain or compel relevant information (e.g., criminal authorities). Many jurisdictions have established procedures domestically for sharing information about manipulative activity between the relevant parties/authorities.

#### **1. Cooperation between exchanges**

In some jurisdictions, exchanges may be in a primary position to detect and prevent manipulative activity. This is because some exchanges have self-regulatory responsibilities whereby each exchange monitors the daily activities of its market and supervises its market and participants to ensure compliance with domestic laws and regulations. Such exchanges are viewed as being in an advantageous position to monitor for manipulative activities and to share relevant information proactively with other affected exchanges. Thus, sharing of market surveillance information and other exchange-to-exchange cooperation play important roles in combating manipulation.

Exchanges may have the ability to share information informally with one another or on a case-by-case basis. Under such informal arrangements, exchanges may notify each other of manipulative activity proactively or upon request. There may be formal mechanisms under which exchanges share information. One example of such formal mechanisms is the Intermarket Surveillance Group (ISG)<sup>10</sup>.

The ISG provides a framework under which exchanges share information regarding related products and market surveillance, and otherwise coordinate regulatory efforts. The ISG was created by the major U.S. exchanges as a domestic effort toward sharing information and discussing common regulatory concerns. Since its creation, the ISG has expanded its membership to include major securities exchanges and derivatives exchanges worldwide where these exchanges also have self-regulatory responsibilities.

Participation in the ISG requires a commitment by each member to share with other members information that is useful to the investigation of trading violations. When an ISG member, through conducting market surveillance on its own marketplace, has a reasonable basis for believing manipulation has occurred, that member will review consolidated ISG data to determine if the manipulation occurred across more than one market. If other markets are affected, the member will coordinate an investigation with any other ISG member, as appropriate. This coordination enables members to avoid duplicative efforts.

Information sharing within the ISG is subject to certain conditions. For example, information is shared as needed and upon request. Also, confidential information must be kept confidential and used only for regulatory purposes.

While the ISG is comprised of international members, domestic information sharing also takes place within the membership since several members are located in the same jurisdiction. By sharing such information with other members, exchanges are on alert to potential manipulation and other illegal activity that could affect the markets on a domestic level.

## **2. Cooperation between exchanges and regulators<sup>11</sup>**

Information sharing between an exchange and its regulator plays a crucial role in detecting, investigating and prosecuting manipulative activity. As noted above,

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<sup>10</sup> The following exchanges are members of the ISG: Alberta Stock Exchange, American Stock Exchange, Amsterdam Exchanges, Boston Stock Exchange, Brussels Exchange, Chicago Board Options Exchange, Chicago Stock Exchange, Chicago Board of Trade, Chicago Mercantile Exchange, Cincinnati Stock Exchange, London Stock Exchange, Montreal Exchange, National Association of Securities Dealers, New York Board of Trade, New York Stock Exchange, Pacific Stock Exchange, Philadelphia Stock Exchange, OM Stockholm Exchange, Toronto Stock Exchange, Vancouver Stock Exchange.

<sup>11</sup> TCWG-4 received the assistance of several exchanges and self-regulatory organizations throughout this project. Representatives from the London Stock Exchange, the National Association of Securities Dealers – Regulation, the New York Stock Exchange and the Chicago Board of Trade made presentations to the group concerning their surveillance and enforcement programs.



exchanges may be in an advantageous position to gather market surveillance information and other information on manipulative activity. Some exchanges can use this information to investigate the conduct of their members and take necessary disciplinary action. Where an exchange does not have investigative authority or where the conduct involves a non-member, information gathered by the exchange relating to manipulative activity may be useful to its regulator.

Many exchanges are under statutory obligation to provide information to and otherwise cooperate with their regulators. Such exchanges often work closely with their regulators to assist in building investigations relating to manipulation and other illegal activity. Also, an exchange may have technical expertise and resources that are unavailable to the regulator. In those instances, the cooperation of an exchange contributes greatly to a regulator's efforts to investigate and prosecute violations of domestic securities and derivatives laws.

Where the obligation to provide information does not exist, a jurisdiction should review and amend its legislation to give the regulator the authority to compel such information. This authority is essential for a regulator to gather sufficient information to combat manipulation.

### **3. Cooperation between regulator and other authorities**

There are occasions when authorities that are not securities or derivatives regulators or exchanges hold relevant information. For example, law enforcement, banking and other authorities may possess or have the ability to gather certain information relating to manipulative activity. It may be necessary for regulators to follow special routes to obtain the information from other domestic authorities.

With respect to cooperation between regulators and domestic law enforcement authorities, in some jurisdictions, manipulation can be both a civil/administrative and criminal offense. Often in these jurisdictions, regulators consult regularly with domestic law enforcement authorities and frequently refer cases to each other. They also may share non-public information subject to its confidentiality treatment.

In other jurisdictions, regulators are required to refer manipulation cases to their domestic law enforcement authorities. These regulators' primary role is investigating the manipulative activity, while the criminal authorities have responsibility for the prosecution of such offenses.

### **B. International Cooperation**

Cross-border trading, multiple listings and globalized markets have increased the need for international cooperation in detecting, investigating and prosecuting manipulative activity. Because manipulative activity can easily overcome international borders, it is essential that regulators and other authorities have the ability to share information internationally.

Information sharing internationally may take place pursuant to informal or formal mechanisms. Some authorities have the ability to share information directly with a regulator. In other cases, regulators may be able to access information about manipulative activity indirectly from a third party.

Regulatory cooperation may be enhanced when a regulator has the legislative authority to obtain information on behalf of its foreign counterparts in order to share it with them. This authority may include, for example, a regulator being able to share information in its files in response to a request from a foreign regulator; compel an individual or entity to produce information (e.g., documents or testimony) requested by a foreign regulator; and proactively provide information to the foreign regulator. Often, when negotiating formal arrangements, regulators may be required to confirm that they have legislative authority to assist their foreign counterparts.

## **1. Cooperation between foreign regulators**

Cross-border manipulation creates challenges for foreign regulators. Information necessary to determine whether manipulation occurred or to support an action against manipulative conduct may be located in another jurisdiction. Additionally, investigations in multiple jurisdictions may arise as a result of the cross-border conduct. Consequently, it has been well established that international cooperation is essential to a regulator's efforts to detect, investigate and prosecute cross-border manipulation.

Cooperation can be undertaken informally or pursuant to formal, written arrangements. Generally, effective information sharing requires regulators to ensure that they have the ability to collect, to share information and otherwise to cooperate with their counterparts.

### **a. Memoranda of understanding (MOUs) and other formal arrangements**

Formal arrangements, such as MOUs, do away with the need to negotiate assistance on an ad hoc basis. Formal arrangements provide established mechanisms by which regulators may obtain information on manipulative activity and other offenses from their foreign counterparts. The arrangements may also establish the conditions under which information provided in response to requests is used and to what extent the information must be kept confidential. While the arrangements may not be legally binding, the arrangements express an intention by like-minded parties to use their best efforts to provide assistance to the extent possible under domestic law.

Under these formal arrangements, regulators often make requests to their foreign counterparts to obtain information regarding manipulative activity. The arrangements may also provide procedures under which a regulator can proactively notify a foreign regulator of information of interest. Finally, where there are investigations in multiple jurisdictions relating to the same manipulative conduct, the arrangements may lay the basis for foreign regulators to work closely on their respective investigations.

### **b. Case-by-case arrangements**

Regulators often contact one another to request information and other assistance with cases involving manipulative activity. Many foreign regulators are able and willing to assist their counterparts even in the absence of formal information sharing arrangements.

In considering a request for assistance, foreign regulators may take into account factors such as a requestor's willingness and ability to reciprocate and to keep privileged information confidential. Many times, a foreign regulator will limit use of the information to regulatory purposes or require the requestor to notify the foreign regulator if the information will be used in a manner inconsistent with the original request. A foreign regulator also may require the requestor to sign an undertaking, which requires the requestor to agree to certain conditions in order for cooperation to take place.

## **2. Cooperation between regulator and others**

Frequently, securities or derivatives regulators seek the assistance of their foreign counterparts. However, there are circumstances in which the regulator may need to obtain the information from other authorities, such as foreign law enforcement authorities. For example, there may be no securities or derivatives regulator in the foreign jurisdiction, or if one exists, it may not have the power to compel the production of information on behalf of a foreign regulator. In such cases, the involvement of other foreign authorities may be helpful.

Cooperation between securities and derivatives regulators and other types of authorities is important. There are instances where information may be shared directly between regulators and other foreign authorities. In other instances, different mechanisms may be used.

### **a. Direct cooperation**

Some regulators have been able to work directly with foreign authorities in matters involving manipulation. For example, in some jurisdictions, legislation explicitly allows a foreign authority to assist regulators. In other jurisdictions, language in legislation is interpreted to allow authorities to share information with a foreign regulator.

### **b. Indirect arrangements**

Regulators also can obtain the assistance of foreign authorities indirectly by working closely with domestic authorities. For example, domestic law enforcement authorities on behalf of the domestic regulator can request the assistance of foreign law enforcement authorities through mutual legal assistance channels. Close cooperation between the regulator and its domestic criminal authorities is necessary when the regulator requests information through these channels.

### **c. Assistance through counterpart regulator**

Foreign regulatory counterparts can play an important role in facilitating information sharing between a regulator and a foreign authority. For example, the foreign

counterpart may better understand the regulator's need for cooperation and may have useful contacts with foreign authorities. Also, the foreign counterpart may be able to assist in framing the request to the foreign authorities to make it more likely that a positive response will be received and to expedite the response.

### **3. Cooperation between regulators and foreign exchanges**

There are instances where a regulator may work directly with foreign exchanges in matters involving manipulation. Because regulators sometimes delegate specific supervisory authority to their exchanges, exchanges in the first instance may possess information that their regulators generally may not have on file. Some exchanges are legally permitted and willing to share such information with foreign regulators.

Where a foreign exchange does not have the authority to share information on manipulative activities directly with a foreign regulator, it may be possible to obtain the foreign exchange's assistance indirectly through the exchange's regulator. The exchange's regulator may have the authority to request or to compel the information from the exchange on behalf of the requesting regulator.

The Declaration on Cooperation and Supervision of International Futures Exchanges and Clearing Organizations (Boca Declaration), March 1996, and the accompanying MOU provides a multilateral framework for cooperation between exchanges and foreign regulators, including information sharing regarding possible manipulative activity. The Boca Declaration encourages international information sharing among exchanges, clearing organizations and regulators and plays a significant role in addressing cross-border manipulative activity.

### **4. Cooperation between foreign exchanges**

Where manipulative conduct affects multiple jurisdictions, information sharing between an exchange and its foreign counterpart is one mechanism for detecting and combating cross-border manipulation. Exchanges that have the authority to survey their markets may be in the best position to monitor for manipulative activity through such surveillance. Accordingly, these exchanges also may be in the best position to notify other jurisdictions immediately of manipulative activity affecting their markets.

Some exchanges have the ability to share information informally with foreign exchanges either upon request or proactively. Additionally, negotiated arrangements for exchange-to-exchange cooperation exist and can provide procedural mechanisms by which information may be shared. Two examples of such arrangements include the Companion Memorandum of Understanding to the Boca Declaration and the ISG.

#### **a. Companion MOU to the Boca Declaration**

The exchange MOU that accompanies the Boca Declaration constitutes an international, multilateral arrangement for sharing information on a bilateral basis between the requesting and requested derivatives exchanges and clearing organizations consistent

with their legal and contractual obligations. The documents establish mechanisms whereby the occurrence of certain agreed triggering events relating to an exchange member's financial resources or positions will permit the sharing of information upon request under the MOU. The trigger levels are designed to facilitate the identification of large exposures by firms that could have a potentially adverse effect on markets.

The Boca Declaration itself serves as an acknowledgment by supervisory authorities that regulated exchanges may ask them to make information available to another supervisory authority where appropriate, and may be requested to facilitate exchange-to-exchange information sharing in instances where laws impede an exchange from communicating with a counterpart directly.

#### **b. ISG**

As noted above, the ISG provides a multilateral framework for cooperation between exchanges with self-regulatory responsibilities, including information sharing regarding possible manipulative activity. Because the ISG encourages information sharing among its international membership, the ISG plays an important role in facilitating international efforts to combat manipulation. When one member detects potential cross-border manipulative activity, the ISG provides procedures through which the member can notify its foreign counterparts and coordinate investigations.

### **VIII. RECOMMENDATIONS**

Securities and derivatives regulators charged with enforcing laws, regulations and rules that prohibit manipulative conduct should have:

- effective tools to prevent and detect manipulation, including laws that proscribe manipulation with sufficient clarity and flexibility to allow prosecution of novel manipulative schemes ;
  - adequate authority to investigate, prosecute, and deter market manipulation and/or the ability to work with other domestic authorities that investigate, prosecute and deter market manipulation ; and
  - the ability to cooperate at all stages of a matter — from surveillance, through investigation, to commencement of an action — across markets and across borders.
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## **ANNEX 1: SUMMARY OF MANIPULATION SUBMISSIONS**

### **(Submissions from TCWG-4 members)**

#### **I. AUSTRALIA: Australian Securities and Investments Commission (ASIC)**

##### A. Conduct Prohibited :

1. There are two prohibitions relating specifically to securities markets manipulation:

- The Corporations Law prohibits the carrying out of transactions which have, or are likely to have, the effect of raising, lowering, or stabilizing the price of those securities on a stock market, with the intention of inducing other people to buy or sell those or related securities. The prohibition is on causing an artificial price, with the intention of inducing trading (the causing of the artificial price is not sufficient, there must also be an intention to induce the relevant conduct).
- The Corporations law also prohibits the creation of a false or misleading appearance with respect to the market for, or the price of, securities. Without limiting the general prohibition, false or misleading appearance is deemed to have been created in circumstances where there is no change in beneficial ownership or where there are matched sales.

2. There are also two prohibitions with respect to futures markets :

- The Corporations law prohibits the carrying out of futures transactions which have the effect of creating an artificial price on futures markets in Australia.
- The Corporations law also prohibits the creation of a false or misleading appearance of active dealing or with respect to the market for, or price of, futures and the carrying out of fictitious transactions. The provision specifically states that in determining whether a transaction is fictitious or artificial, the fact that the transaction was intended to have effect according to its terms is not conclusive.

##### B. Source of Prohibition:

1. Sections 997 and 998 of the Corporations Law
2. Sections 1259 and 1260 of the Corporations Law

##### C. Standard(s) of Proof :

1. Criminal Proceedings: beyond a reasonable doubt
2. Civil Proceedings: balance of probabilities

D. Other Relevant Authorities:

1. The Corporations Law section 999 prohibits a person from making a statement or disseminating information that is false or misleading in a material particular, and which is likely to induce other persons to deal in securities or affect the price of securities, where the person does not care whether the statement or information were true or knows or ought reasonable to have known that it was false or misleading.
2. Section 995 provides a general prohibition on false or misleading conduct in connection with any dealing in securities (civil remedies only).
3. The Business Rules of the Australian Stock Exchange Limited and the Sydney Futures Exchange, which apply to members, also prohibit manipulative practices.

E. Available Sanctions:

1. Violation of the market manipulation provisions of the Corporations Law can result in criminal sanctions including fines and imprisonment of up to 5 years.
2. Civil remedies include injunctions, freezing the proceeds of transactions, and declaratory orders. There is no power to impose a fine or other pecuniary penalty. Damages may be claimed by persons who suffer loss as a result of manipulative conduct.
3. Administrative action (including loss of license/banning from industry) can be taken against licensed entities that engage in market manipulation. The exchanges may also take action against their members.

F. Note :

A current law reform proposal (part of the Corporate Law Economic Reform Program) would harmonize the laws in relation to securities and futures. It is proposed that there would be three basic prohibitions:

- conduct which influences the price of securities or derivatives with the intention of inducing others to deal in the securities or derivatives ;

- creation of a false or misleading appearance of active trading in securities and derivatives. If the conduct is undertaken with an intent to defraud it will constitute a criminal offense; without the necessary intent it will be a civil offense ;
- carrying out fictitious transactions which have the effect of maintaining, inflating or depressing the price of securities or derivatives. If done with the intent to defraud it will constitute a criminal offense; contravention without the intention to defraud will result in civil liability.

The law reform proposal also suggests the introduction of a civil pecuniary penalty.



## **II. CANADA – ONTARIO - Ontario Securities Commission (OSC)**

### A. Conduct Prohibited :

1. Under the Criminal Code of Canada “*every one who, by deceit, falsehood or other fraudulent means, whether or not it is a false pretense within the meaning of this Act, with intent to defraud, affects the public market price of stocks, shares, merchandise or anything that is offered for sale to the public is guilty of an indictable offense...*”
2. The Criminal Code of Canada also expressly prohibits wash trading and match trading, when done with the intent to create a false or misleading appearance respecting public trading or market price.

### B. Source of Prohibition :

Criminal Code of Canada, R.S.C. 1985, c.C-46, section 380(2)  
 Criminal Code of Canada, R.S.C. 1985, c.C-46, section 382

### C. Standard(s) of Proof:

The standard of proof under the Criminal Code of Canada is “beyond a reasonable doubt”.

### D. Other Relevant Authority :

1. The Securities Act (Ontario), R.S.O. 1990, c.S.5, sec.1.1(b) provides that the OSC has the statutory objective to “*foster fair and efficient capital markets and confidence in the capital markets.*” Under this provision, the Commission has the authority to issue orders in the public interest.
2. Section 11.26 of the Toronto Stock Exchange General By-laws prohibits members from knowingly participating in manipulative trading activity.
3. The Criminal Code of Canada authorizes police to investigate manipulative trading practices. Criminal Code of Canada, R.S.C. 1985, c.C-46, sections 380(2) and 382.

### E. Available Sanctions :

1. Market manipulation prosecuted under the Criminal Code of Canada carries a maximum term of 10 years imprisonment.

2. Wash trading and match trading prosecuted under the Criminal Code of Canada carry maximum penalties of 5 years imprisonment.
3. The OSC can suspend or terminate registration, suspend or terminate trading exemptions, order that all trading in a security cease and order that a director or officer resign their position and/or be prohibited from acting in such a capacity in the future. The OSC can also apply to the courts for declaratory relief in circumstances where a market participant is not complying with Ontario Securities legislation. Possible relief includes orders to rescind transactions, orders to make restitution, and orders to pay damages.
4. For specific violations of the Ontario securities law, the OSC can initiate quasi-criminal proceedings in the courts that can result in jail sentences of up to two years and/or a fine of up to \$1 million (or more if convicted of insider trading).
5. Self-regulatory organizations (SROs), such as the Toronto Stock Exchange, can initiate administrative hearings that can result in the suspension or expulsion of a member. The TSE can also halt trading in the issuer's security and suspend or delist the issuer.

### **III. CANADA - QUEBEC - Commission des Valeurs Mobilières du Québec (CVMQ)**

#### A. Conduct Prohibited:

1. Under the Canadian Criminal Code, every one who, by deceit, falsehood or other fraudulent means, whether or not it is a false pretence under the Criminal Code, with intent to defraud, affects the market price of, inter alia, stocks or shares, is guilty of an indictable offense.
2. The Criminal Code sets out the offense of manipulation of stock exchange, curb market or other market transactions. Every person who uses one of these institutions with intent to create a false or misleading appearance with respect to the market price or trading activity of a security, and who (1) carries out a securities transaction that involves no change in beneficial ownership, (2) enters an order for the sale of a security knowing that a substantially matching or counterbalancing purchase order has been or will be entered on behalf of the same or different persons, or (3) enters an order for the purchase of a security knowing that a substantially matching or counterbalancing sale order has been or will be entered on behalf of the same or different persons is guilty of an indictable offense.

#### B. Source of Prohibition :

1. Section 380(2) of the Canadian Criminal Code (R.S.C., chap. C-46)
2. Section 382 of the Canadian Criminal Code (R.S.C., chap. C-46)

#### C. Standard(s) of Proof :

The standard of proof under the Criminal Code of Canada is “beyond a reasonable doubt.”

#### D. Other Relevant Authorities :

1. The Québec Securities Act contains no specific manipulation offense, but gives the CVMQ a broad supervisory mandate which includes the protection of investors against unfair, improper, and fraudulent practices.
2. Rule 6306 of the Montréal Exchange By-laws and Rules prohibits members from engaging in manipulative or deceptive trading methods.

E. Available Sanctions :

1. Market manipulation under Section 380(2) carries a maximum term of 10 years imprisonment.
2. Wash trading and match trading under Section 382 carry maximum penalties of 5 years imprisonment.
3. The CVMQ may order that all trading in a given security cease and/or that the registration of a given dealer be suspended or cancelled. Moreover, the CVMQ can initiate penal proceedings resulting in fines ranging from \$5,000 to \$1 million dollars where the value or the market price of a security is likely to be affected by a misrepresentation in a prospectus, financial statement, press release or other specified documents.
4. Exchange disciplinary actions can result in sanctions including the suspension or expulsion of a member.

F. Note :

A proposed amendment to the Quebec Securities Act would enable the CVMQ to impose administrative penalties (not exceeding \$100,000) on registrants for manipulation-related violations.

#### IV. FRANCE -- Commission des Opérations de Bourse (COB)

##### A. Conduct Prohibited :

Market manipulation can be prosecuted before the courts as a criminal offense (“délit”). Further, the COB also has the authority to seek administrative action for violations (“manquements”) of the COB’s Rules or Regulations.

##### 1. Under criminal law, it is considered manipulative conduct

*«The act, for any person, of conducting or attempting to conduct, directly or by a third person, a manoeuver with the intention to impede the normal functioning of a market of financial instruments, by misleading others».*(article 10-3 of the September 28, 1967 Ordinance)

The communication of false information is a distinct offense that is also criminally prosecuted.( article 10-1 §3 of the 1967 Ordinance). It is :

*«The act, for any person, of knowingly spreading to the public, by whatever channels and means, false or deceitful information on the prospects or status of an issuer whose securities are traded on a regulated market or on the future prospects of a financial instrument listed on a regulated market, of such a nature as to influence prices».*

##### 2. The COB also has the authority to impose administrative sanctions. Under its Rule n° 90-04, relating to price setting :

*«The purpose of orders transmitted on the market shall be neither to hinder the setting of prices on the market, nor to mislead others».* (article 3)

Under its Rule n° 98-07, relating to the obligation to inform the public,

*«For all persons, the disclosure of inaccurate, imprecise or misleading information shall be considered to be in breach of the obligation to provide proper information to the public. Likewise, the disclosure of such information knowingly shall be considered to be in breach of the obligation to provide proper information to the public».* (article 3)

##### B. Source of Prohibition:

1. Criminal sanctions :

For market manipulation : Law of July 22, 1996 which modifies Article 10-3 of the September 28, 1967 Ordinance.

For false information : Law of July 22, 1996, which modifies Article 10-1 of the Ordinance of 1967.

2. Administrative sanctions :

COB's Rule n° 90-04, relating to price setting

COB's Rule n° 98-07, relating to the obligation to inform the public.

C. Standard(s) of Proof:

Before the Law of July 22, 1996, Article 10-3 (criminal sanctions) required that a party “knowingly” engage in the prohibited conduct. Despite the fact that the explicit reference to ‘knowing’ conduct has been removed, there is still a “scienter” requirement to the criminal offense. However, there is no specific intent or “scienter” element to conduct that will trigger administrative actions and sanctions.

D. Other Relevant Authority :

The Rules of ethics established by the Conseil des Marchés Financiers (Council of Financial Markets) stipulate that intermediaries must follow certain principles relating to transparency, security, fairness and integrity (Law of July 2, 1996, article 58).

E. Available Sanctions :

1. Criminal offenses are prosecuted before criminal courts by the public prosecutor and can result in sanctions including up to two years imprisonment and a fine up to ten times the profits realized or 10 million francs, for individuals. The fine cannot be fixed at an amount less than the profit realized. For companies, the maximum fine is five times the amount stated for individuals. Other available sanctions include closure of the company, banishment from trading on the markets and the publication of the indictment in the newspapers.

3. Administrative sanctions for violation of the COB regulations may be in the form of a fine of up to 10 million francs, or, where profits are made, up to ten times the profits realized (Law of August 2, 1989, which modifies Article 9-2 of the 1967 Ordinance).

## **V. GERMANY -- Bundesaufsichtsamt für den Wertpapierhandel (BAWE)**

### A. Conduct Prohibited:

Criminal liability attaches to “any person who, in order to manipulate the exchange or market price of securities, subscription rights, foreign currency, commodities, interests granting a right to participate in the profits of an enterprise, or derivatives, within the meaning of section 2 II WpHG.

1. makes false statements with respect to circumstances material to the valuation of the securities, subscription rights, foreign currency, commodities, interests granting a right to participate in the profits of an enterprise or derivatives, or conceals such facts in violation of existing regulations, or
2. employs other means with the intent to deceive.

### B. Source of Prohibition :

Section 88 of the German Exchange Act (Börsengesetz)

### C. Standard(s) of Proof :

Pursuant to Section 88 the precondition for a punishable crime is a deliberate act, in which it is sufficient if the perpetrator is aware that his activity leads to a manipulation of the exchange and market prices, whether he desires it or not.

Furthermore, it is required that the perpetrator acted with the intention to exert influence on the exchange and market prices. The intention to influence prices is sufficient, the corresponding success need not occur.

### D. Other Relevant Authorities:

The department of public prosecution has power to prosecute criminal offenses under Section 88 of the German Exchange Act.

In addition, far-reaching powers of investigation and intervention have been assigned to the exchanges in the context of their self-regulation in order to ensure the proper conduct of operations and price determination.

In Germany supervision of security trading is allocated in three jurisdictions : the Bundesaufsichtsamt für den Wertpapierhandel, the exchange supervisory authorities of the German states (Länder) and the stock exchange itself as a self regulatory body.

E. Available Sanctions :

Under criminal law a infringement of the regulation of Section 88 may be punished by imprisonment of up to three years or a fine.

In the context of their self-regulation the stock exchanges may also impose disciplinary measures to its members and registered traders (e.g. exclusion from trading or revoking the admission of an official broker).

F. Notes:

In the context of the Fourth Financial Market Promotion Act the amending of material facts of price manipulation is being discussed. The details of the alteration have yet to be settled.



## **VI. GREECE : Capital Market Commission**

### A. Conduct Prohibited :

Under Hellenic legislation price manipulation through certain practices is prohibited and both criminal and administrative sanctions are imposed to the violators by the competent authorities.

### B. Source of Prohibition :

There are several provisions in Hellenic Law under which price manipulation can be caught, namely article 34 of Law 3632/1928, article 72 par. 1 and 2 of Law 1969/1991, the provisions of the Presidential Decree 53/1992 on Insider Dealing and the Ministerial Decision on the Code of Conduct for Investment Firms.

More specifically, under article 34 of Law 3632/28 a person who uses any practices capable to mislead the public by influencing the prices of securities traded on Stock Exchanges for the purpose of making illicit profit will be punished with imprisonment and a fine.

Without prejudice to the criminal sanctions, the Capital Market Commission (CMC) may impose fines which amount up to GRD 100.000.000 (approximately USD 363 thous.) to entities supervised by it.

Under article 72 par. 1 of Law 1969/1991, a person who disseminates deliberately false or inaccurate information through the press or by any other means, which may influence the price of one or more securities traded in Stock Exchanges, will be punished with imprisonment and a fine up to GRD 100.000.000 (approximately USD 363 thous.).

Under article 72 par. 2, as amended by article 96 of Law 2533/1997, the CMC may impose fines which amount up to GRD 500.000.000 (approximately USD 1818 thous.) to natural or legal persons that publish or divulge by any means inaccurate or misleading information relating to transferable securities listed in an organised exchange and that information may influence the price or the transactions of such securities.

Manipulative practices, may also be caught under P.D.53/1992 which enacted into domestic legislation the Insider Dealing Directive. The above P.D. prohibits transactions in securities by any person who has access to information because of his profession, employment or duty and obtains information relating to these securities which is not made public and if made public could have an effect on prices of these securities.

More specifically, P.D. 53/92 prohibits the acquisition or disposal of, for his own account or for the account of a third party, transferable securities of the issuer to

which that information relates. The persons covered by this prohibition are the persons who possess inside information by virtue of their membership in the administrative, management or supervisory bodies of the issuer, their holdings in the capital of the issuer or because they have access to such information by virtue of the exercise of employment, profession or other duties as well as any other person who with full knowledge of the facts possesses inside information, the direct or indirect source of which could not be other than the persons described above.

It should be noted that the definition of inside information includes information that relates to one or several issuers or one or several transferable securities.

Consequently, the inside information may relate only to transferable securities and not necessarily to the issuer of those securities. For this reason, article 3 of the P.D. 53/92 provides that the persons covered by the prohibition are not restricted to persons who participate or have access to the administrative bodies of the issuer, but includes as well any person who possesses inside information by virtue of his holding in the capital of the issuer.

Under par. 4.3.d of the Code of Conduct for Investment Firms, the investment firm should not effect any transactions or other acts of which it is aware or should be aware that they aim to the distortion of the securities market, are based on inside information in breach of relevant provisions or otherwise directed against the credibility or the integrity of the market.

Under article 7 of the Law 2396/1996 the CMC may impose to the investment firms that violate the above provision a fine up to GRD 50.000.000 (approximately USD 182 000).

C. Standard(s) of proof :

- 1.
2. **As specified in the above provisions.**

D. Other relevant authorities :

None.

E. Available sanctions :

Administrative sanctions for violation of administrative provisions and criminal sanctions where a criminal violation is established.

## **VII. HONG - KONG -- Securities and Futures Commission (SFC)**

### A. Conduct Prohibited:

Criminal anti-manipulation rules prohibit :

1. The creation of a false or misleading appearance of active trading of a particular security on the Hong Kong Stock Exchange ("SEHK");
2. The creation of a false market on the SEHK in which the market price of a particular security is raised or depressed or pegged or stabilized by means of:
  - a. Sales and purchases transacted by persons acting in collaboration with each other for the purpose of securing a market price for a particular security that is not justified by the fundamentals of the company;
  - b. Any act which has the effect of preventing or inhibiting the free negotiation of market prices for the purchase or sale of the security; or
  - c. The employment of any fictitious transaction or devices or any other form of deception or contrivance.
3. Any purchase or sale of a particular security which involves no change in the beneficial ownership of that security and which is conducted with the intention of depressing, raising or causing fluctuations in the market prices of that security; and
4. The dissemination of information to the effect that the price of a particular security on the SEHK will rise or fall because, to the disseminator's knowledge, someone is creating a false or misleading appearance of active trading in that security or a false market in respect of that security.

### B. Source of Prohibition :

Section 135, Part XII of the Securities Ordinance

### C. Standard(s) of Proof :

Criminal Proceedings : beyond a reasonable doubt

D. Other Relevant Authorities :

1. Section 138 of the Securities Ordinance prohibits, for the purposes of inducing the sale of securities of any corporation, the dissemination of any statement with respect to those securities or with respect to the operations, or the past or future performance of the corporation which the disseminator at that time know or has reasonable ground to believe to be false or misleading.
2. Rule 545 of the Rules of the SEHK prohibits exchange members from participating in acts proscribed under section 135 of the Securities Ordinance. Members who fail to comply with the rules are liable to disciplinary action by the SEHK Council.

E. Available Sanctions:

1. Violation of any of the provisions of Sections 135 and 138 of the Securities Ordinance is a criminal offense that can result in a fine of up to \$50,000 and 2 years imprisonment.
2. The Securities and Futures Commission ("SFC") is also empowered, under Rule 9 of the Statutory Listing Rules to direct the suspension of a security traded on the SEHK. However, this rarely happens as companies are often urged to seek voluntary suspension, based on encouragement by either the SFC or the SEHK.
4. Disciplinary proceedings brought by the SEHK for a breach of Rule 545 may result in sanctions against a member including suspension of membership.

## **VIII. ITALY -- Commissione Nazionale per le Società e la Borsa (CONSOB)**

### A. Conduct Prohibited :

Market manipulation consists of spreading false, exaggerated or misleading information or setting up simulated transactions or other devices that are likely to have significant effects on the price of securities or to give the appearance of an active market in such securities.

### B. Source of Prohibition :

Articles 181 to 187 of the Act on Financial Markets (Legislative Decree No. 58/1998)

### C. Standard(s) of Proof :

The authority has not to prove the specific intent or « dolo » in manipulating the market

### D. Other Relevant Authorities :

No other authorities, without prejudice of the general competence of the Criminal Public Prosecutor

### E. Available Sanctions:

Market manipulation is a criminal offense and is punished by up to three years imprisonment and a fine between 1million and 50 million lire. If the price of securities involved changes significantly or the appearance is given of an active market the Court will increase the penalties. The penalties should be doubled if the market manipulation is

#### 1. committed by

- shareholders who exercise control over the company;
- directors of the company whose securities are involved;
- liquidators, general managers, auditors of firms engaged in investment business;
- stockbrokers
- members or employees of CONSOB; or

#### 2. committed through the press or other mass media.

Conviction entails suspension of business activities and the exercise of public functions for between six months and two years.

## **IX. JAPAN -- Securities and Exchange Surveillance Commission (SESC)**

### A. Conduct Prohibited:

1. To spread a rumor, use a deceptive device, resort to violence or intimidate another person in connection with the purchase or sale of, or other forms of trading in, a security, or to do such things with the aim of causing a change in the price of a security.
2. To sell (or buy) a security without intending to transfer rights thereby creating a misleading appearance of active trading (wash sale).
3. To sell (or buy) a security in collusion with another person who buys (or sells) the same security at the same time and price (matched order).
4. To create, alone or jointly with others, a misleading appearance of active trading in a security, to effect a series of trades of a security to cause a change in the price of the security, or to place or accept an order for such trades.

### B. Source of Prohibition :

1. Section 158 of the Securities and Exchange Law
2. Section 159(1)(1)-(3) of the Securities and Exchange Law
3. Section 159(1)(4)-(7) of the Securities and Exchange Law
4. Section 159(2) of the Securities and Exchange Law

### C. Standard(s) of Proof :

There is no specific standard of proof, but generally cases must be proved "beyond reasonable doubt."

### D. Other Relevant Authorities :

Various conduct that could lead to market manipulation is also prohibited under the rules of self-regulatory organizations such as stock exchanges or securities dealers associations.

### E. Available Sanctions :

Violation of the market manipulation provisions of the Securities and Exchange Law can result in fines of up to five million yen and/or imprisonment of up to five years.

Manipulation with the intent to obtain money or other property can result in sanctions including fines of up to 30 million yen and/or imprisonment of up to 5 years.



## **X. MEXICO -- Comision Nacional Bancaria Y De Valores (CNBV)**

### A. Conduct Prohibited:

1. In general terms, securities legal framework strictly prohibits to carry out unhealthy market activities with regard to specific manipulative prices.
2. Sanctions are contemplated for those who disseminate wrongful information regarding an issuer obtaining a benefit from such information.
3. Brokerage firms are prevented from carrying out customer orders that involve unhealthy trading methods or any other transaction forbidden by law, regulation or stock exchange rules.
4. Intermediaries in derivatives are prohibited from : (i) entering into a Contract or in the purchase or sale of an underlying asset with the purpose to simulate an activity, (ii) altering the prices or conditions of the transactions they enter into or the registration of the terms of such transaction and (iii) distorting the process of price formation, interrupting the orderly operation of the Market, or causing an artificial increase in the quotation of an underlying asset or a contract listed in the Exchange.

### B. Source of prohibition :

1. Securities Market Act (20 III, 26 Bis 8, 35 and 37).
2. Securities Market Act, (52 Bis 2).
3. Securities Market Act, (96).
4. Derivatives Exchange Rules (3003).

### C. Standard(s) of Proof :

Through different means including relevant documents, testimonies, etc.

### D. Other Relevant Authorities ("Provisions") :

1. The Securities Market Act also :
  - Requires that brokerage houses keep adequate trading control systems.
  - Grants the CNBV the authority to approve and modify existing securities contracts.
2. Circulars (regulation) issued by the CNBV include :

- The ability of the CNBV to promote healthy and balanced securities market developments.
- The duty for brokerage houses to trade in accordance with the securities legal framework, as well as under healthy market practices.
- The responsibility of brokerage houses for using modern trading and settlement systems.
- The obligation to issuers to disseminate relevant information.
- The rules for valuation of stock prices and the CNBV's power to impose a veto on a specific valuation.

3. Mexican Stock Exchange Rules set :

- The ability of the Stock Exchange to request additional information to an issuer regarding relevant events.
- The ability of the Stock Exchange to request information pertaining to an issuer regarding relevant events in case of sudden price fluctuation.
- The powers of the Exchange Officer in charge of the trading session to deny or cancel matched trades when the intermediaries do not comply with healthy market practices.
- The guidelines for the calculation of closing prices.

4. Mexican Securities Industry Ethics Code. This code encompasses the following main principles :

- To act in accordance with the securities legal framework and healthy market practices.
- To act professionally in order to develop an orderly and transparent market.
- To create a customer-oriented culture, thus generating confidence.
- To avoid conflicts of interest.
- To promote disclosure of information.
- To safeguard customer's confidential or other privileged information.
- To compete in a proper and efficient manner.

E. Available Sanctions :

1. Registration in the National Registry of Securities and Intermediaries may be cancelled if an intermediary carries out transactions that do not conform to healthy market practices.
2. Violation of Article 52 Bis-2-I may lead to imprisonment up to five years and fines up to three times the obtained benefit.
3. The Mexican Stock Exchange may suspend either brokers or floor traders involved in unhealthy trade transactions.
4. The Derivatives Exchange may cancel the operation in the derivatives market of the intermediaries that constantly violate the Derivatives

Exchange provisions. Monetary penalties may also be imposed to such intermediaries.

**XI. NETHERLANDS -- Stichting Toezicht Effectenverkeer (STE)**

## A. Conduct Prohibited :

1. Under the Dutch Penal Code, criminal liability is attached to a person who, with the intention to unlawfully favor himself or another person by spreading false information by which the price of commodities, funds or securities is influenced.
2. Price manipulation and other misleading acts are prohibited under the Further Regulation on the Supervision of Securities Trade Act, which applies to licensed securities institutions such as brokerage firms and portfolio managers. Specifically, the Act requires that securities institutions refrain from misleading actions including misrepresentations concerning securities, the trading of securities or by influencing transactions in financial instruments of others by means of providing misleading information as well as by carrying out one or more securities transactions.

## B. Source of Prohibition :

1. Section 334 of the Dutch Penal Code
2. Article 32 of the Further Regulation on the Supervision of Securities Trade Act (effective February 1999).

## C. Standard(s) of Proof :

1. There is no experience in prosecuting violations of Section 334 of the Penal Code. Under this provision elements such as "intent" and "unlawful" have to be proven.
2. "Misleading actions" as described in section 32 have to be determined.

## D. Other Relevant Authorities

Section 7(c) of the regulations of the Amsterdam Exchanges, which covers trading on the exchange and is binding on members, contains a similar provision but does not have the requirement that one favor himself or another person unlawfully to commit price manipulation.

## E. Available Sanctions:

1. Criminal: imprisonment (2 years) or fine (DFL 100 000).
2. Administrative: instructions, withdrawal of the licence, administrative fine (DFL 20 000) or penalty.

F. Note :

The Minister of Finance and Securities Board of the Netherlands have publicly endorsed adjustments to manipulation laws in the Netherlands so that they will correspond to provisions in other countries. One amendment that may become law in 2001 would extend non-criminal manipulation laws to everyone, not just securities institutions.

## **XII. NORWAY -- Kredittilsynet**

### A. Conduct Prohibited :

No one may seek by fraudulent means to influence the price of a financial instrument that is quoted on a Norwegian stock exchange.

Fraudulent influence is deemed to include the spreading of incorrect or misleading information, or entering into spurious agreements for the purpose of:

1. influencing someone to subscribe for, purchase, or sell financial instruments, or rights to financial instruments, or to abstain from doing so;
2. influencing the subscription price; or
3. influencing the conversion ratio in connection with merger or dissolution of companies.

Both willful and negligent conduct may represent a violation of the prohibitions.

### B. Source of Prohibition :

Section 2-6 of the Securities Trading Act.

### C. Standard(s) of Proof :

Beyond any reasonable doubt.

### D. Other Relevant Authority :

1. Price manipulation may also constitute a violation of Section 2-5 of the Securities Trading Act (Prohibition against unreasonable business methods), which provides as follows :
  - No one may employ unreasonable business methods when trading in financial instruments.
  - Good business practice shall be observed in approaches to the general public or to individuals which contain an offer or encouragement to make an offer to purchase, sell or subscribe for financial instruments or which are otherwise intended to promote trade in financial instruments.
2. Section 273 of the Criminal Code (1902) provides as follows :

Those who spread incorrect or misleading information to influence the price of goods, securities or other items, or contribute to such actions, are punished with imprisonment up to four years. Fines can be given in addition to imprisonment. In case of very extenuating circumstances, fines alone can be given.

3. Section 274 of the Criminal Code (1902) provides that :

... those who[,] in a request of participate in the foundation or expansion of a joint stock company or other company with economic purpose, or in taking over loans given to such company, give incorrect or misleading information that is of significance for the evaluation of the company can be sentenced to up to four years imprisonment].

The same punishment can be given to a representative or employee of such company if he publishes incorrect or misleading information that is of significance for the evaluation of the company, or give such information to the company's participants or creditors, any of the company's internal bodies or to a public authority. The same applies for others who due to assignments for the company have knowledge of its activities....

E. Available Sanctions :

1. Violation of section 2-6 of the Securities Trading Act can lead to fines or imprisonment of up to six years.
2. Violation of section 2-5 of the Securities Trading Act can lead to fines or imprisonment of up to one year.
3. Violation of sections 273 or 274 of the Criminal Code can lead to fines or imprisonment of up to four years.

### **XIII. PORTUGAL -- Comissao do Mercado de Valores Mobiliarios (CMVM)**

#### A. Conduct Prohibited :

##### 1. Market manipulation

*Actus reus:* Market manipulation consists of spreading false, incomplete, exaggerated or misleading information or setting up transactions with fictitious nature or other fraudulent practices carried out by one or more physical persons and suitable to hamper the regular functioning of any markets, including over-the-counter market.

Under the law, any conducts that might create artificial prices, affect the demand or supply of a security or of any other financial product or in any way may harm the demand or supply in a public offering, are deemed suitable to hamper the regular functioning of securities markets.

##### 2. Violation of the duty to put an end to manipulative conducts

*Actus reus:* The members of the board of directors and the persons responsible for the management and control of financial service providers having acknowledged market manipulation practices as mentioned above, carried out by people under their responsibility, are obliged to put an end to such practices.

##### 3. *Mens rea* (in both crimes)

General intention to engage in or to fail to put an end to manipulative conducts is requested (article 14 of the Penal Code).

#### B. Source of Prohibition:

Article 379<sup>o</sup>/ 1, 2 of the Securities Code (Decree Law 486/1999).

#### C. Standards of Proof:

Beyond any reasonable doubt.

#### D. Other Relevant Dispositions:

Article 311<sup>o</sup> of the Securities Code, under the reference “market protection”, generally provides that financial service providers must refrain from engaging in any practice that hampers the regular functioning of the market, its transparency and credibility. Any manipulative conducts carried out by corporate entities and any reckless practices, carried out by physical persons or by corporate entities, will also be deemed unlawful under this disposition.



The conducts deemed to be unlawful include but are not limited to the following :

- Setting up transactions in which there is no change in actual ownership of securities ;
- Apparent, simulated or artificial transactions of securities between different securities portfolios ;
- Setting up transactions to limit or defraud the market rules regarding the acquisition of securities ;
- Setting up transactions to foment or to stabilize operations which were not registered or approved by the CMVM.

Therefore, spreading of information which is not complete, true, actual, clear, objective and lawful (article 389<sup>o</sup>/1); carrying out non permitted transactions or to carry out transactions in non permitted conditions (article 395<sup>o</sup>/1/b)); as well as engaging in any practice that hampers the regular functioning of the market, its transparency and credibility (article 398<sup>o</sup>/d)) are deemed unlawful.

The CMVM may carry out preliminary investigations in what concerns market manipulation, in order to gather the evidence needed for the Criminal Authorities to prosecute its authors (Articles 382<sup>o</sup> to 387<sup>o</sup> of the Securities Code).

#### E. Available Sanctions:

##### 1. Criminal Sanctions

- Market manipulation is punished with up to three (3) years imprisonment or with a criminal fine. Attempted market manipulation is punished with up to two (2) years imprisonment or with a fine.
- The members of the board of directors and the persons responsible for the management and control of financial service providers that have violated the duty to put an end to manipulative conducts are punished with up to two (2) years imprisonment or up to a two hundred and forty (240) days criminal fine, if no heavier penalty is applicable under the law.

##### 2. Administrative Sanctions (applicable when article 311<sup>o</sup> is violated) :

- Administrative fines from a minimum of Euro 25.000 to a maximum Euro 2.500.000 are applicable, under article 388<sup>o</sup>/1/a) of the Securities Code (“common dispositions” – very serious sanctions ).
- Accessories sanctions

The administrative sanctions may be cumulated with the following accessories sanctions (article 404<sup>o</sup> of the Securities Code) :

- a. apprehension and loss of the gains obtained with the forbidden conducts
- b. temporary interdiction up to five (5) years of carrying out the activity normally performed by the perpetrator.
- c. prohibition of carrying out functions up to five (5) years as director, manager or supervisor and of representing any financial service provider in any financial service activities.
- d. publication in suitable places of the administrative sanctions applicable, paid off by the perpetrator.
- e. revocation, suspension or conditioning of the license of the registrant;

Articles 109<sup>o</sup> to 112<sup>o</sup> of the Penal Code generally provide that the instruments, profits and products obtained through criminal action are either lost in favor of the Portuguese State or are returned to its rightful owners.

### 3. Civil Sanctions

Those injured by any manipulative conducts, or by the violation of the duty to put an end to such conducts, may ask for compensation of damages in the criminal procedure carried against the persons or entities responsible (article 71<sup>o</sup> of the Penal Procedure Code).

Those injured by any manipulative conducts that haven't asked for compensation of damages in criminal procedure, may benefit from the conviction decision obtained in such procedure to reverse the burden of proof in their favor to achieve such compensation (article 674<sup>o</sup>-A of the Civil Procedure Code).

### 4. Provisional remedies

Any injured person may ask the court to seize any assets or to set a cash bond in their favor (articles 227<sup>o</sup> and 228<sup>o</sup> of the Penal Procedure Code).

#### **XIV. SPAIN -- Comisión Nacional del Mercado de Valores (CNMV)**

##### A. Conduct Prohibited:

1. Securities price manipulation (very serious infringement) is defined as practices intended to falsify the free establishment of prices while affecting significantly the quotation and provoking important damages to investors.
  2. Securities price manipulation (serious infringement) is defined as practices intended to falsify the free establishment of prices that cannot be considered very serious infringements.
  3. Penal law provisions prohibit scheming to alter prices. The following criteria may be borne in mind in determining the existence of market manipulation :
    - Conduct detected that has a manipulative effect, consisting of the creation of a false or misleading impression either about the existence of an active market for the security or about the price of the security.
- The conduct must be performed with a manipulative intent to prompt others to do or refrain from doing something based on false appearances.

##### B. Source of Prohibition :

Article 99, paragraph i and article 100, paragraph w of the Securities Market Act.

Article 284 of the Penal Code.

Comparative law principles.

##### C. Standard(s) of Proof :

Criminal procedures: Beyond any reasonable doubt.

Administrative procedures: Preponderance of the evidence.

##### D. Other Relevant Authorities :

The imposing of sanctions for extremely serious infringements shall rest with the Minister of Economy and Finance at the proposal of the CNMV after a report from its Consultative Committee, except for the cancellation of an approval, which shall be imposed by the Council of Ministers (Article 97 of the Securities Markets Act 24/1988).

In those cases where manipulation has a criminal nature the Public Prosecutor and Criminal Courts shall be involved.

E. Available Sanctions :

The Law 37/1998 of November 16 amended the Securities Markets Act of 1998 and, for the first time, distinguished manipulative conduct as either a “very serious infringement” or a “serious infringement.” Under the new designation, the following sanctions are available :

According to Article 102 of the Securities Markets Act, one or more of the following sanctions shall be imposed upon the offender committing extremely serious infringements :

- a. A fine of no less than the amount of the gross profit obtained as the result of the actions or omissions of which the infringements consists and no more than five times the amount; or, in the event that this criterion is inapplicable, up to the greater of the following resulting amounts : 5% of the offender’s equity ; 5% of the total funds, belonging to the offender or borrowed, used in the infringement ; or 50 million pesetas.
- b. Suspension or restriction of the type or volume of transactions or business which the offender may carry out in the securities market for a period not exceeding five years.
- c. Suspension of membership of an official secondary market for a period not exceeding five years.
- d. Cancellation of the approval in the case of investment services firms, management companies of the Public Debt Market represented by book entry or other entities registered with the C.N.M.V.. In the case of affiliates of investment services firms authorized in other States members of the European Union, this cancellation sanction will be substituted by the prohibition of trading new operation on the Spanish territory.
- e. Public admonition with publication in the Official Journal “Boletín Oficial del Estado”.
- f. Removal from office and disqualification from holding managerial or executive office with the same institution for a term not exceeding five years.
- g. Removal from office and disqualification from holding managerial or executive office in any other financial institution of the same kind for a term not exceeding ten years.

All the sanctions imposed for extremely serious infringements will be published in the Boletín Oficial del Estado (the Official Journal) once they are firm.

In addition to the respective sanction imposed on the offender for the perpetration of extremely serious infringements, when the offender is a corporation, one of the following sanctions may be imposed upon those holding managerial or executive offices therein who are responsible for the infringement :

- a. A fine of up to the greater of the following figures: 5% of the total funds, belonging to the offender or borrowed, used in the infringement or 50 million pesetas.
- b. Suspension from office for a term not exceeding three years.
- c. Removal from office and disqualification from holding managerial or executive office with the same institution for a term not exceeding five years.
- d. Removal from office and disqualification from holding managerial or executive offices in any financial institution, or related one, for a term not exceeding ten years.

The imposing of sanctions for serious infringements shall rest with the C.N.M.V., that can impose one or more of the following:

- a. Public admonition, with publication in the Official Journal.
- b. A fine up to the amount of the gross profit obtained as the result of the actions or omissions of which the infringement consists. In the event that this criterion is inapplicable, up to the greater of the following amounts:
  - 2% of the offender's equity.
  - 2% of the total funds belonging to the offender or borrowed, used in the infringement.
  - 25 million pesetas.
- c. Suspension or restriction of the type or volume of transactions or business which the offender may carry out in the securities market for a period not exceeding 1 year.
- d. Suspension of membership of an official secondary market for a period not exceeding 1 year.
- e. Suspension of managerial office for a period not exceeding 1 year in the firm committing the offence.

In addition to the respective sanction imposed on the offender for the perpetration of serious infringements, when the offender is a corporation, one of the following sanctions may be imposed upon those holding managerial or executive offices therein who are responsible for the infringement:

- a. Public admonition, with publication in the Official Journal.
- b. A fine of up to the greater of the following:
  - 2% of the total funds, belonging to the corporation or borrowed, used in the infringement.
  - 25 million pesetas.
- c. Suspension from any executive office in that entity for a term not exceeding one year.

## **XV. SWEDEN -- Finansinspektionen**

### A. Conduct Prohibited:

1. The Criminal Code provides that a person who publishes or otherwise disseminates misleading information among the public in order to influence the price of an article, a security, or other property, shall be sentenced for swindling to imprisonment for at most two years or, if the crime is petty, to a fine or imprisonment for at most six months.

Also, a person who assists in organizing a share company or other firm or who, because of his position ought to possess special knowledge about a firm, intentionally or through gross carelessness publishes or otherwise disseminates misleading information among the public or among those holding an interest in the firm which is likely to influence the assessment of the firm from a financial point of view, and thereby causes damage, shall be sentenced in accordance with the paragraph immediately above.

2. The Financial Instruments Trading Act (1991:980) provides that any person who, in conjunction with trading on the securities market, with the intention of unduly influencing the price in conjunction with public trading in financial instruments:
  - a. concludes agreements or takes any other action as a sham; or
  - b. secretly makes the transfer of financial instruments subject to an undertaking to later acquire such at a given lower price or subject to terms and conditions which limit the right of further transfer or otherwise are intended to exclude the instrument from public trading.

The aforementioned shall also apply where any person, in circumstances other than those referred to in the first paragraph, in conjunction with trading on the securities market, with the intention of unduly influencing the price of publicly-traded financial instruments, enters into a buy or sell agreement, submits an offer for the conclusion of such agreement, adopts any other similar measure, or causes any other person to take such action and where such measure is intended to mislead buyers and sellers of financial instruments.

### B. Source of Prohibition:



1. Criminal Code; Chapter 9, Section 9.
2. Financial Instruments Trading Act (1991:980); Chapter 7, Section 1.

C. Standard(s) of Proof:

The prosecutor has to prove the criminal act and the subjective requirements-  
“beyond a reasonable doubt”

D. Other Relevant Authorities :

According to the Securities Exchange and Clearing Operations Act (SFS 1992:543) Chapter 4, Section 2. “A securities exchange (and an authorised marketplace) shall maintain appropriate rules and regulations which govern trading on the exchange.

The securities exchange shall supervise trading and price formation on the exchange and shall ensure that trading is carried out in compliance with this Act and other legislation and in accordance with sound trading practices for securities markets.

The securities exchange shall, upon request by the Financial Supervisory Authority, afford the Authority terminal access to its system for the monitoring of trading and price trends.

Section 8. A securities exchange shall possess a disciplinary committee charged with the task of handling breaches by members and issuers of the securities exchange regulations.

E. Available Sanctions:

1. If a crime as defined in Criminal Code is grave, imprisonment for at least six months and at most six years shall be imposed.
2. Under the Financial Instruments Trading Act, one found guilty of undue price influence can be ordered to pay a fine, or sentenced to a term of imprisonment not exceeding 2 years.

Where, taking into consideration the scope of the effect on the price or other circumstances, the crime is deemed to be aggravated, such a person shall be sentenced to a term of imprisonment of not less than 6 months and not more than 4 years.

A person shall not be sentenced in accordance with this section where the crime is subject to penalties pursuant to the Penal Code or the violation is minor.

3. The disciplinary committee of an exchange may impose disciplinary measures to the members or issuers (fine, expulsion, reprimand).

## **XVI. SWITZERLAND -- Swiss Federal Banking Commission (SFBC)**

### A. Conduct Prohibited :

1. The Penal Code (criminal law) prohibits price manipulation which is a criminal offense.

Under criminal law price manipulation is defined as follows :

Whoever, with the intention of influencing in a material manner the price of securities traded in Switzerland on stock exchanges in order to gain therefrom unlawful economic advantage for himself or third parties, disseminates, against one's better knowledge, misleading information or effects purchases and sales of such securities which are undertaken on both sides directly or indirectly for the account of the same person or persons who are related for this purpose, will be punished...

2. The SFBC has the authority to impose administrative sanctions to the bodies which are under its supervision (i.e. banks and securities dealers), based on a general provision contained in both the Banking Act (BA) and the Securities Act (SESTA) which provide that the responsible employees have to guarantee the proper conduct of the business operations.

### B. Source of Prohibition :

Section 161<sup>bis</sup>, Price rigging (or price manipulation), of the Swiss Penal Code; art. 3/2/c BA and art. 10/2/d SESTA regarding the proper conduct of business operations, as far as banks or securities dealers are concerned .

### C. Standard(s) of Proof :

The rules discussed above have only recently entered into force so there is not yet sufficient case law to describe in detail the appropriate standard(s) of proof.

Generally, under criminal law both elements "intention" and "unlawful economic advantage" are necessary. The information disseminated must also be misleading. Despite the restrictive appearance of this standard, the Supreme Court seems to have taken a more expansive view of what should be a punishable behavior.

Under the administrative point of view, the "proper conduct of operations" has to be determined on a case-by-case basis by the SFBC. The elements which can be taken into account are not necessarily the same and can be applied in a less

restrictive way. From the SFBC's point of view, a distinction between the penal (art. 161bis PC) and the administrative (art. 6 SESTA) price manipulation can be made so that supervisory rules may cover a wider range of price and market manipulation activities than criminal law.

D. Other Relevant Authorities :

Cantonal penal authorities and Federal Supreme Court as far as criminal prosecution is concerned.

The Swiss system is based on self regulation so that the stock exchange itself has to issue the rules—which are submitted to the approval of the SFBC—for effective and transparent trading and are also responsible for the supervision of the trading, and specially for the discovery of price manipulation under the high supervision of the SFBC. This is a two step system with an authority (SFBC) and a self-regulatory body (the stock exchange).

E. Available Sanctions:

Criminal prosecutions can result in Imprisonment or a fine. Administrative sanctions from SFBC range from reprimand to withdrawal of the authorization.

The Swiss Exchange may also impose disciplinary measures to its members and registered traders (reprimand, suspension, expulsion, fine up to 10 million CHF).

## **XVII. UNITED KINGDOM -- Financial Services Authority (FSA)**

### A. Conduct Prohibited:

Prohibited conduct includes :

1. Knowingly or recklessly making statements, promises or forecasts that are misleading, false or deceptive or the dishonest concealment of any material fact for the purpose of inducing others to enter, or refrain from entering an investment agreement or to exercise or refrain from exercising rights conferred by an investment.

This prohibition applies provided:

- the statement, promise or forecast is made in or from, or the facts are concealed in or from, the UK;
- the person on whom the inducement is intended to or may have effect is in the UK; or
- the agreement is or would be entered into or the rights are or would be exercised in the UK.

2. Any course of conduct that creates a false or misleading impression as to the market in or the price or value of any investment for the purposes of creating that impression and thereby inducing another person to acquire, dispose of, subscribe for or underwrite those investments or refrain from doing so or to exercise or refrain from exercising any rights conferred by those investments.

This prohibition applies where:

- the Act is done or the course of conduct is engaged in the UK; or
- the false or misleading impression is created in the UK

### B. Source of Prohibition:

Section 47 of the Financial Services Act 1986 ("FSAAct 1986")

### C. Standard(s) of Proof:

In criminal proceedings for an offense under section 47, the criminal standard of proof applies—the jury must be satisfied “beyond a reasonable doubt” or “satisfied so that they are sure.”

In civil proceedings for an injunction or restitution order, the civil standard of proof applies—the court must be satisfied that it is more likely than not that the person breached section 47. However, as breach of section 47 is also a criminal offense, the civil court is likely to require weighty evidence to establish a breach. A similar standard of proof applies in SRO or exchange disciplinary proceedings.

D. Other Relevant Authorities:

1. The UK Department of Trade and Industry, the Serious Fraud Office and the Crown Prosecution Service have power to prosecute criminal offenses under section 47 in England and Wales. The FSA has no power at present to bring criminal proceedings with respect to market manipulation offenses, although such a power is proposed in the draft Financial Services & Markets Bill.
2. The FSA has power under section 61 of the FSAct 1986 to bring civil proceedings for injunctions and restitution orders with respect to breaches of section 47.
3. FSA Statements of Principle requiring that all authorized firms should observe “high standards of market conduct” and “high standards of integrity and fair dealing.”
4. Exchange rules contain specific prohibitions against manipulative activity by their members.

E. Available Sanctions:

A person convicted in criminal proceedings of an offense under section 47 FSAct 1986 may be sentenced to up to seven years imprisonment, a fine, or both.

Under section 61 FSAct 1986, injunctions and restitution orders may be obtained with respect to breaches of section 47.

A breach of the FSA Statements of Principle by an authorized firm may be disciplined under the relevant self-regulatory organization’s rules—the available sanctions include regulatory fines, public censure and withdrawal of authorization or an individual’s registration. Similarly, the exchanges may discipline breaches of their rules by their members.

F. Note :

There are proposals for reform of financial services regulation which include new measures to combat market manipulation. Aspects of these proposals include:

1. Civil prohibitions against market abuse affecting markets on recognized investment exchanges. These will apply to both regulated and unregulated persons. The prohibitions are likely to be framed in general terms and will complement existing criminal offenses with respect to market manipulation and insider trading.
2. The FSA will be given the power to issue a Code of Market Conduct that will likely contain specific provisions regarding price manipulation, abusive squeezes and corners, artificial or fictitious trades, and the dissemination of misleading information as well as provisions in relation to the misuse of privileged information.
3. Under the proposed legislative reform, where there has been a breach of the new provisions, the FSA will have administrative powers to require the disgorgement of profits, restitution and the payment of civil fines. The exercise of these powers will be subject to a right of appeal to a new independent specialist tribunal. The FSA will be given power to bring criminal proceedings with respect to offenses of market manipulation and insider dealing.

**XVIII. UNITED STATES -- Commodity Futures Trading Commission (CFTC)**

A. Conduct Prohibited:

1. Section 6 of the Commodity Exchange Act (“CEA”) authorizes the Commission to sanction any person who is manipulating, is attempting to manipulate, or has manipulated the market price of any commodity or futures contract.
2. Neither the CEA nor the Commission’s regulations, however, define the term “manipulation.” Commission precedent establishes that manipulation entails engaging in intentional conduct which results in an artificial price, i.e., a price that does not reflect the basic forces of supply and demand. There are four essential elements to be established under the CEA to prove manipulation :
  - a. that the accused had the ability to influence market prices;
  - b. that he or she intended to influence market prices;
  - c. that artificial prices existed; and
  - d. that the accused caused the artificial prices.

B. Source of Prohibition:

- |           |           |                                                                     |
|-----------|-----------|---------------------------------------------------------------------|
| <b>B.</b> | <b>1.</b> | <b>Section 6 of the Commodity Exchange Act, 7 U.S.C. § 8 (1994)</b> |
| <b>C.</b> |           |                                                                     |
| <b>D.</b> | <b>2.</b> | <b>Court and Commission precedent</b>                               |

C. Standard(s) of Proof:

**IX. CIVIL: PREPONDERANCE OF THE EVIDENCE (I.E. MORE LIKELY THAN NOT ACCUSED INTENDED TO CAUSE ARTIFICIAL PRICES).**

Criminal: Beyond a reasonable doubt.

D. Other Relevant Authority:

1. Section 9 of the CEA, 7 U.S.C. § 13 (1994), imposes criminal liability for manipulations or attempted manipulations, corners or attempted corners, or transmission of false or misleading reports concerning information or conditions that affect or tend to affect the price of any commodity in interstate commerce.



2. Section 5(4) of the CEA, 7 U.S.C. § 7(4) (1994) allows the CFTC to license an exchange as a contract market only where the exchange's governing board has provided for the "prevention of manipulation of prices and the cornering of any commodity by the dealers operators of such boards."
3. Section 5a(4) of the CEA, 7 U.S.C. § 7a(4) (1994), authorizes the Commission to extend exchange delivery periods where to do so "would prevent or tend to prevent 'squeezes' and market congestion endangering price stability."
4. Section 4c(a) of the CEA, 7 U.S.C. § 6c(a) (1994), provides that it is unlawful for any person to offer to enter into, enter into, or confirm the execution of any wash sale, cross trade, accommodation trade, fictitious sale, or any transaction used to cause any price to be reported, registered, or recorded which is not a true and bona fide price.
5. SRO/Exchange Rules

E. Available Sanctions :

1. Administrative Cases :
  - Cease- and-desist orders
  - Revocation, suspension or conditioning of the license of a registrant with the CFTC
  - Prohibiting a respondent from trading on Commission-regulated markets
  - Assessment of civil penalties of up to \$110,000 per violation or triple the monetary gain
  - Restitution to customers of damages proximately caused by the respondent's violations
2. Civil Injunctive Proceedings:
  - Injunction of illegal conduct by court order;
  - Equitable relief such as restitution and disgorgement
  - Civil monetary penalties
3. Criminal Sanctions:
  - Market manipulation or attempted manipulation may also be prosecuted by the US Department of Justice as a felony. Under the Act, a felony conviction for price manipulation can result in a fine of up to \$1,000,000 (\$500,000 for an individual) or up to five years imprisonment, or both.

**XIX. UNITED STATES -- Securities and Exchange Commission (SEC)**

## A. Conduct Prohibited :

Manipulation is intentional interference with the free forces of supply and demand for a security, often designed to deceive or defraud investors through controlling or artificially affecting the price of securities or market activity.

## B. Source of Prohibition:

1. Section 17(a) of the Securities Act of 1933, which prohibits manipulative conduct in the offer and sale of securities.
2. Section 9(a) of the Securities Exchange Act of 1934 ("1934 Act"), which contains prohibitions against manipulation of securities prices.
3. Section 10(b) of the 1934 Act, which regulates the use of manipulate and deceptive devices or contrivances.
4. Rule 10b-5 of the 1934 Act, which provides generally that it shall be unlawful for any person: to employ any device, scheme, or artifice to defraud; to make any untrue statement of a material fact or to omit to state a material fact; or to engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.
5. Section 15(c) of the 1934 Act, which prohibits manipulative conduct by brokers and dealers engaging in securities transactions in the over-the-counter market.

## C. Standard(s) of Proof :

1. Civil: preponderance of the evidence
2. Criminal : beyond a reasonable doubt

## D. Other Relevant Authority :

None specified.

## E. Available Sanctions :

1. Administrative Cases:

- Cease- and-desist orders
- Revocation, suspension or conditioning of the license of a registrant
- Prohibiting a respondent from trading on Commission-regulated markets
- Assessment of penalties against a regulated entity
- Orders to disgorge unlawful gains

2. Civil Injunctive Proceedings :

- Injunction of illegal conduct by court order
- Equitable relief such as restitution and disgorgement
- Civil monetary penalties

3. Criminal Sanctions :

Market manipulation or attempted manipulation may also be prosecuted by the US Department of Justice as a felony.

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**X. ANNEX 2 : EXAMPLES OF METHODS USED IN SOME**  
**XI. INTERNATIONAL MANIPULATION CASES UNCOVERED IN**  
**XII. THE JURISDICTIONS OF THE MEMBERS OF TCWG-4**

The following examples have been provided by members of TCWG-4, and relate to manipulation cases that have been uncovered in the respective jurisdictions. The examples involve transactions or other activities carried out in two or more securities markets. These markets may be within the same jurisdiction (cross-market cases) or in different jurisdictions (cross-border cases).

**XIII. I. CONVEYING FALSE OR FRAUDULENT INFORMATION**

**A. SEC v. Huttoe, et al. (SEC – U.S.A.)**

A case currently pending in the U.S. District Court for the District of Columbia gives an example of manipulation of a stock traded in the US over-the-counter market. The issuer was a company that had a video teleconferencing product. The primary defendants in the case included the chairman of the issuer's board of directors and two paid promoters. The promoters received stocks directly from the issuer for recommending the stock to the readers of their newsletter.

The manipulation was carried out through the issuance of false press releases and the touting of the stock in the newsletter. The newsletter was published daily to over 700 subscribers, and was disseminated, among other ways, over the Internet via a limited access World Wide Web site. The ability to disseminate information quickly to subscribers was a significant factor in carrying out the manipulation. After the price of the stock had been driven up through the dissemination of false and misleading information about the company, its contracts, and its prospects, the defendants sold their own holdings and made large profits.

As a measure to avoid or at least slow down SEC's detection and tracing of such trading, and perhaps to evade taxes, two of the defendants used corporate shells, incorporated in the Bahamas, and opened brokerage accounts for their Bahamian entities in Canada. Much of the illegal trading was conducted through these Canadian accounts.

**B. SEC v. Cavanaugh, et al. (SEC – U.S.A.)**

Another case from the SEC gives an example of manipulation carried out through a combination of dissemination of false and misleading information and cornering of the market (securing such relative control of a financial instrument that its price can be manipulated). The scheme resulted in an artificially inflated share price at which the defendants sold millions of shares and realized large profits. The issuer was a company specializing in the development of fingerprint verification products, and its shares were traded on the NASD OTC Bulletin board.

Person A was a partner and 50% owner of US Milestone, an investment advisory firm. In December 1997, three Spanish entities opened accounts with a US registered broker-dealer on the recommendation of A. Soon thereafter, US Milestone bought a large quantity of shares in company B at 4 cents per share. At the time these shares were thinly traded, and the purchase constituted a large percentage of the existing shares. US Milestone deposited these shares into the brokerage accounts maintained by the Spanish entities.

A few days later, while the shares were traded at 50 cents per share in the open market, A places orders with a Canadian broker for the shares at \$5.00 per share. As a result, the share price rose more than 1.000% in one day. And the Spanish entities maintained the artificially high share price for several months by controlling the supply of the stock, while during the same time, the issuing company B disseminated false and misleading information about its products and customer orders. Indeed, company B had yet to produce a commercially viable product. Company B also filed misleading forms with the SEC.

Between December 1997 and March 1998, the stock held by the Spanish entities was sold to the public at prices between \$5.00 and \$6.50 per share. From this scheme, the defendants realised profits of over \$10 million, of which over \$5 million was transferred to Spain. Some of these proceeds were then transferred from Spain to accounts in Switzerland.

The SEC sued 32 defendants and obtained a preliminary injunction in U.S. federal district court to stop the ongoing manipulation, and obtained freeze orders and an order requiring the defendants to repatriate the illegally obtained proceeds. The SEC also received the assistance of criminal authorities in Spain and Switzerland to freeze the proceeds located in their jurisdictions.

### **C. Case related to dissemination of false information (COB - France)**

Although French law prosecutes false information dissemination as separate from price manipulation, an example from COB in France has been included. The COB is currently investigating a case related to the market of shares of a French company. This company carries out an important part of its activity with an American company. It appears that the latter would like to make the French company less attractive as it is targeting this company. In this respect, the American company:

- Developed an Internet site posting various false and misleading messages regarding the activity of the French company (in particular, messages indicating that the French company was involved in several lawsuits and that it had not taken into account the financial costs of these trials within its financial results...)
- Contacted several press media, including a French daily newspaper, in which it made public the Internet address of the above mentioned site and gave some “ negative ” commentaries regarding the targeted French company.

The manipulative techniques involved:

- Using an electronic medium such as the Internet,

- Dissemination of false and misleading information, over the Internet and in the financial press, with the objective of provoking a downward trend of the share price of the targeted French company.

## **1. II. MARKET ACTIVITIES THAT CREATE THE APPEARANCE OF ACTIVE TRADING.**

### **A. Wash Sales – sales in which there is no change in actual ownership of the security – cross-border cases**

#### **1 - Nomura-case (ASIC – Australia and SFC – Hong Kong)**

This case involved the participation of Hong Kong registered persons in the Nomura Group, attempting to artificially depress the price of constituent stocks of the Australia All Ordinaries Index at the close of the trading session on the expiry date of the relevant futures contracts. The aim of depressing the price of the stocks, was to drive down the value of expiring futures on the index. Manipulation was carried out by a combination of aggressive selling near the close of the trading on the Australian Stock Exchange on the expiry date, and a placement of a “Bid Basket” at prices well below market levels. The sell orders “hit” the bids, and there was a sale of shares without any change of beneficial ownership.

In December 1998, the Australian Federal Court handed down a judgement finding that Nomura had manipulated both the securities and futures markets in Australia - including that it had intended to create a misleading appearance of active trading in securities and a false or misleading appearance with respect to price for dealings in contracts in the futures market.

#### **2 - Paramount Portugal - case (CMVM – Portugal)**

An unauthorized Swiss company, although not active in Switzerland, provided investment services through an unauthorized Portuguese branch, offering shares in several foreign companies having no activity or value. To create the illusion of market activity related to the shares one of these inactive companies, the owners of the unauthorized investment-firm quoted transactions on the NASD OTC Bulletin Board between legal persons that were wholly owned or controlled by themselves. These transactions falsely indicated that there was a market demand for the shares at a certain price, thus providing the investment firm with “documentation” for the offering-price for the shares.

The public prosecutor of Portugal has accused Paramount Portugal of several unlawful actions, such as carrying out investment business without the necessary authorization and other forms of fraudulent actions leading to economic losses for investors. The criminal proceedings took place in the fall of 1998 and led to a conviction of 9 years of imprisonment of the company’s manager.

At the same time, the company headquarters in Switzerland were put into liquidation, pursuant to an administrative decision of the supervisory authority. This decision was based on the statement that the company’s investments

services in securities dealings did not comply with the relevant rules of conduct, especially the duty of loyalty. Inquiries are also undertaken by the Swiss Judicial Authorities and the US SEC in this context.

**B. Wash sales combined with other manipulative activity**  
**a. Case related to cross-market manipulation in French markets (COB – France)**

In this case, a French credit institution made several transactions on the French futures market on the 3-Month Pibor contract between December 1994 and February 1995. The said transactions were carried out through different brokers. More precisely the trades consisted of several cross trades (« applications » in French) for a proprietary trading account of a credit institution. According to French legislation on the futures market, a cross trade should be a matching of orders by a market member of two clients' orders for a specific contract. This matching:

- should not be induced,
- should be made within the range of bids and asks available on the market.

The investigation conducted revealed that :

1. The two affiliated branches transactions were initiated by the same trader at the same moment.
2. The transactions were made in order to alter the range of bids and asks available on the market. The trades were also made to quote prices (bids and hits) at different prices than the last quoted ones in order to give the appearance of legitimate or active trading.
3. The trades were also made to influence the price of the contract at the end of the trading session and alter the compensation price of the contract.
4. The suspicious orders were repeated several times within the period under review and represented quite an important percentage of the market for that contract at that time.

The investigation was conducted thanks to all the powers vested in the COB's investigators, notably :

1. The acquisition and analysis of all market documents and internal brokerage documents,
2. The acquisition and analysis of taped records from intermediaries, and
3. The acquisition of testimonies of persons questioned.

At the investigation's conclusion, the case was transmitted to the French Public Prosecutor on the basis of price manipulation, for final judgement. The case is currently under review. The breach of Regulation 90.04 as to price setting was stated as the basis of the report written by the COB's Enforcement Department, which resulted in an administrative sanction procedure being initiated.

**C. Matched orders**

**XIV. DELTA CASE (CMC – GREECE)**

*(This example is a domestic case relating to only one market.)*

On November 6, 1996 the brokerage firm "Delta Securities" failed to meet its obligations towards the clearing house (the Central Securities Depository) and failed, leaving an exposure of GRD 2.5 billion (approximately USD 9,1million). As there existed no insurance mechanism for the immediate finance of the GRD 2.5 billion gap at that time, the settlement system of the Stock Exchange faced major difficulties. An emergency legislative act of the Government was required in order to provide emergency finance and restart the settlement process.

The crisis of November 1996 spurred many regulatory actions of the CMC (protection from systemic risks, transparency, investor protection). The Commission also undertook a massive investigation of exchange members and practices, the largest ever carried out in Greece.

A consortium of three international audit firms was formed and a special legal team was put in place. Each of 65 brokerage firms was examined in terms of financial position, and thousands of transactions in shares were investigated. The Commission questioned tens of brokerage firms and individuals in the process of the investigation.

The basic findings of the widespread investigation were a large-scale scheme of stock manipulation. This scheme attempted to artificially increase or maintain prices of the shares by means of prearranged transactions at agreed prices, by controlling supply and demand, and by attempting to recycle liquidity from sales into purchases of the same shares in an ever widening cycle of transaction growth and financial exposure.

According to the findings of the investigation during the period from October 1995 to April 1996 the price was raised from GRD 380 to GRD 1030. From May 1996 until November 1996 the price reached a maximum of GRD 1300. On April 1996 P.T., the leader of the group, acquired 10 % of the shares and thus he obtained an adequate control of supply that enabled him to realize his objective, i.e. to raise the marketability and the price of the shares.

The basic practice used by the persons involved, was matched sales with a view to increase or stabilize the price through low volume transactions.

In the particular case, the persons involved: a) had information of precise nature which was related to the securities, b) they knew that these securities were subject to an agreement for the inflation of the volume of the transactions and c)



as shareholders of a substantial number of shares controlled supply. Some of the persons involved had also full knowledge that the transactions effected in their names were effected for the account of another person and for this reason were fictitious.

Furthermore, this information was not made public and it is probable that if made public, it would influence the price of the shares, since the price was a result of the false inflation of the transactions and those transactions were of substantial size.

After lengthy legal analysis and administrative due process, the Commission imposed the following sanctions related to this case:

Two brokerage licenses were revoked and four brokerage firms were fined with amounts ranging from GRD 30 to GRD 600 million (approximately USD 109 thous. to USD 2,2 million) each.

Another three brokerage firms received administrative warnings and were placed on special surveillance for three months. They were released from that condition in late 1997, when the Commission was satisfied that they were fully complying with regulations on market conduct and transparency.

Nineteen individuals were found to be involved in severe price manipulatory practices, artificial transactions, and to have abused confidential information; they were fined with varying amounts. Total fines imposed on individuals amounted to around GRD two billion (approximately USD 7,3 million).

Seventeen individuals were found to have committed penal infractions of the law regarding price manipulation, abuse of confidential information, and spreading of false information. The Commission instituted penal proceedings against those individuals.

Finally, the Commission also took penal action against "Delta Securities" and its Directors since it was found that the firm had become a strategic manager of the large-scale manipulatory schemes described.

The actions of the Commission and the regulations which were put in place in the aftermath of the crisis of November 1996 resulted in the return of confidence to the Athens Stock Exchange and enabled the spectacular performance of the Exchange which worked without flaw throughout 1997".

## **XV. III. MARKET POWER MANIPULATIONS**

### **A. Cornering of market involving cross-market manipulation**

#### **A. *In re Fenchurch (CFTC – U.S.A.)***

The U.S. Commodity Futures Trading Commission ("CFTC") has provided an example involving cornering carried out through cross-market manipulation. CFTC filed and simultaneously settled an administrative action against Fenchurch

Capital Management, Ltd (Fenchurch). In an order accepting the firm's offer of settlement in which Fenchurch neither admitted nor denied the findings, the CFTC found that Fenchurch attempted to, and did, manipulate the value of its position in the Chicago Board of Trade's ("CBOT's") Ten-Year U.S. Treasury Note futures contract by cornering the available supply of the cheapest-to-deliver notes.

According to the CFTC's order, Fenchurch increased its position in the issue through a series of transactions in the repurchase market when the notes were in tight supply. Fenchurch exacerbated the tightness in the supply of the cheapest-to-deliver note by increasing its position and intentionally withholding the notes from the market with no legitimate economic purpose. As a result, the shorts on the futures contract were unable to obtain sufficient quantities of the notes and had to deliver a more valuable security.

The CFTC's action against Fenchurch and its underlying investigation were coordinated with the US Securities and Exchange Commission and the CBOT, both of which initiated proceedings of their own. In the CFTC proceeding, Fenchurch was ordered to pay a civil penalty of \$600,000 and to comply with several undertakings intended to guard against similar misconduct in the future. These undertakings included the imposition of enhanced reporting requirements for two years and a requirement that Fenchurch evaluate and strengthen its system of internal controls and supervision.

**B. Cornering of market involving cross-border manipulation**

**1 - In re Sumitomo (CFTC – U.S.A.)**

In May 1998, the CFTC issued an order instituting proceedings, making findings, and imposing remedial sanctions upon Sumitomo Corporation of Japan (Sumitomo). In the order, which accepted an offer of settlement in which Sumitomo neither admitted nor denied the findings, the CFTC found that Sumitomo engaged in a scheme to manipulate the price of copper. In the wake of accumulating large losses from speculative trading, the principal copper trader for Sumitomo engaged in a scheme, in conjunction with an entity operating in the United States, with the intent of manipulating the price of copper.

In particular, during 1995 and 1996, Sumitomo, acting through its agent or agents, established and maintained large and dominating futures positions in copper metal on the London Metals Exchange ("LME"). In the fall of 1995, Sumitomo stood for delivery on a significant percentage of its maturing futures contracts. It thereby acquired a dominant and controlling cash and futures market position which directly and predictably caused copper prices, including prices on the United States cash and futures markets, to reach artificially high absolute prices. This position also created a large backwardation in which the price of the commodity for near-term delivery stood at a premium to the price of the commodity for deferred delivery. Sumitomo intentionally exploited these artificially high prices in order to profit on the liquidations of its large portfolio of futures contracts and holdings of LME warrants. Through these actions, Sumitomo manipulated the price of copper and copper futures in violation of statutory regulations.

The CFTC ordered Sumitomo to cease and desist from further violations of those provisions of the Act and to pay a total of \$150 million. Of that amount, \$125 million was paid as a civil monetary penalty immediately. The penalty is believed to be the largest ever imposed by an agency of the United States government. The remaining \$25 million was placed into escrow for a period of up to four years. During that period, the money may be used to provide restitution to persons injured by Sumitomo's unlawful conduct. If the money has not been paid out for that purpose by the end of four years, it will become part of the civil monetary penalty and be paid to the United States Treasury.

The settlement also requires Sumitomo to cooperate with the CFTC in any further investigations or proceedings related to the conduct at issue. The settlement is the product of an ongoing investigation in which the CFTC benefited from extensive international cooperation. Since the investigation of the copper market events involved information and activity outside our respective jurisdictions, the CFTC, UK Financial Services Authority (formerly the SIB and SFA) and Japanese government worked closely together.

(a) 2 - Cross-border manipulation case from COB - France

The following case is an example of a cross-border investigation on manipulative conduct, involving regulators essentially in France and Great Britain, although this case also involved the Spanish market.

A few years ago, an investment firm liquidated an important fund of stock portfolios concerning in particular, several French securities. To do this, the firm sold the fund of stock portfolios to a bank at a predetermined rate, the bank then took care of the resale. In the course of events, the convened transfer price was to be the rate quoted on the market at a specific hour (12:30 local time), on a predetermined date for the transfer.

However on the said liquidation date and time, a massive sale of these shares on the French market led to a sharp decline in the value of the price per securities share. Thus resulting in a much smaller total sum for the stock portfolio than expected by the firm initially selling.

The investigation conducted revealed that, the person responsible for trading at the London bank having bought the stock portfolio, had irregularly acquired knowledge of the transaction between the bank and the investment firm. This trader anticipated and sold the stock portfolio upon acquiring the certainty of the concluded formal transaction. The COB gathered the information concerning the French broker working at the English bank's branch in France, thus enabling the English authorities to conduct a fruitful investigation. Furthermore, two hearings (to gather information) were carried out, both in the presence of FSA investigators.

In France, the COB transmitted the case to the CMF, which administered an important monetary sanction to the French intermediary. This market authority monitors and gives disciplinary sanctions for unprofessional market misconduct.

In England, the SFA imposed the payment of a monetary compensation by the intermediary to the prejudiced investment firm. The SFA also administered an important monetary sanction on the basis of a price manipulation offence.

## **XVI. IV. OTHER CASES**

### **a. A. Illegal solicitation and fraud in combination with market manipulation (COB – France)**

The COB had decided to investigate the activities of a company located in Spain, after having received complaints from French residents. The company solicited French investors by telephone in order to convince people to purchase shares of an American company listed on a Canadian OTC market. Some of the solicited customers who had invested in this stock stated that they had never seen the shares themselves and that they had experienced difficulties in selling them back.

Materials at the COB's disposal for the investigations included :

- several examples of a confidential letter, which appeared to be sent by the Spanish company through the Dutch post;
- prospectuses about the Spanish company and about the proposed investments ;
- the references of an account opened by the Spanish company at a Belgian bank to collect the funds provided by the clients; and
- the names of several employees and managers from the Spanish company, including those who solicited French customers.

Investigative steps taken by the COB related to :

1. Co-ordination with the Spanish authorities to obtain the most detailed information possible about the Spanish company, its activities, its managers, etc...
2. Co-ordination with American regulators in order to obtain information about the company shares offered to the French public (activities, financial results, managers....)

3. The COB contacted its Belgian counterparts to obtain information about the bank accounts opened by the company under review, within which the money collected from its French investors was apparently deposited. The Belgian counterpart confirmed that money from French residents (19 at the time of this case) was deposited in this account for a total amount of 1.2 million FRF. Other accounts were discovered thanks to the co-operation from the Belgian authorities. This co-operation also permitted the freezing of these accounts through the Belgian Ministry.
4. Simultaneously the COB contacted the Dutch authorities to obtain information about the Dutch office from which the business letters and most mailings were sent to the French residents. The Dutch authorities answered that the firm was not registered with them and that the address was only a mail box.
5. The co-ordination with Canadian authorities to obtain the most detailed information possible about the two stocks traded on the OTC market.

One of the Canadian regulators, the Ontario Securities Commission (OSC), provided the COB with comprehensive details of the transactions performed during the year, the history of the company and of its managers as well as the latest financial statement.

These documents revealed that :

The market value of the company was CDN\$ 73.5 million (more than 2 million shares valued at a market price of CDN\$ 3.5) while the financial statements evidently showed that the company had virtually no assets and had incurred a loss for the last fiscal year. The company seemed to have virtually no activity, and the traded volumes recorded on the market had increased during the few months preceding the investigation.

In the meantime the COB learned that a second stock was proposed to French investors, also traded on the OTC Canadian market. The COB went back to their Canadian counterpart to obtain information on the actual existence of the trades performed on the Canadian market for this second share. The OSC indicated that an investigation was performed at the same time by the Stock exchange on this second stock. The results of this inquiry communicated to the COB concluded a possible case of price manipulation.

International co-operation was remarkable, as well as the manner in which it was performed, during this case. It revealed the importance of co-operation by the intervention of several regulators, acting on different legal infractions and misconducts.

Indeed, in this case, and thanks to the co-operation from different regulators, it appeared that :

- The stocks proposed to the French customers were likely to have been manipulated (financial documents relating to the first stock revealed huge differences between the trading price and the actual value of the company ;

the inquiry conducted by the foreign stock exchange concluded a possible manipulation)

- The trades made on behalf of the customers were not recorded on the market. The stock sellers were not identified. There was no evidence that the trades had ever been performed.
- The two companies, the stocks of which were proposed to customers, were controlled by the same group of persons linked to the Spanish solicitors of the French investors.

The legal infractions included :

- Swindle and/or illegal solicitation of the public (France ; Spain and Belgium for the freezing of funds of French investors)
- Market manipulation (Canada)

It is important to note that the originally investigated misconduct (illegal solicitation of the French public) revealed other market offences, in particular price manipulation. Conversely, this shows that price manipulation can be linked to other fraudulent practices.

This case demonstrates how co-operation efficiency was achieved. Indeed, a case in which the COB had played a key role from the start and for which it had an obvious interest, was concluded more efficiently by actions undertaken by other jurisdictions. Thanks to widely coordinated actions, regulatory authorities in other jurisdictions could take action within their own jurisdiction.

## **B. Case related to an uncooperative jurisdiction (COB – France)**

At the end of a specific market analysis taking place at year end, it was discovered that five stocks had demonstrated a considerable progression in value in uncertain conditions.

- These five stocks had been monitored as having increased by 5% or more almost exclusively with a unique brokerage firm.
- Based on this market trend, the hypothesis of price manipulation was put forward.
- In particular it was found that the buying orders for one of these stocks were made by an offshore international bank, a subsidiary of a French bank which concluded in a 10 % market increase.
- However, the offshore bank authorities refused to answer the COB requests related to its investigation on the grounds of the countries legal constraints regarding information exchanges stipulated in their Secrecy Act. This made it impossible for the COB to obtain the identity of the person giving the

orders, and thus to further investigate a probable case of price manipulation and insider trading under the conditions stipulated in the French 1967 Ordinance.

- In view of this, the COB has forwarded the case concerning these stocks to the Prosecutor's office. The restrictive conditions concerning information exchanges prevalent for the offshore bank in this case illustrates the failure of international co-operation with an offshore center.

### **C - Buying or selling securities or derivative contracts at the close of the market or on the expiry date : the CONSOB's experience**

Typically cases of market manipulation may occur on the expiry date of derivatives contracts and in particular at the quarterly expiry of the index future contract (FIB 30). On these dates, we may see a material variation of the index value during the pre-opening phase of the cash market.

The prices of the securities that compose the basket MIB 30 index are influenced by the arbitrages between the MIB 30 future contract and the underlying securities as well as by the hedge transactions of MIBO 30 market makers.

At the expiry, arbitrageurs on FIB 30, and those having volatile trading strategies on MIBO 30 (buying and selling index options and simultaneously selling or buying the underlying securities) are only interested to execute their transactions, independently on the actual prices. Therefore, they send buy orders or sell orders on MIB 30 securities, with prices close to the maximum limits permitted by variation prices.

Normally bids and asks orders refer to huge transactions on all 30 securities that compose the MIB 30 index. They hit the market simultaneously, causing a sudden unbalanced situation between the buy and sale orders.

The material variation of the index in the pre-opening phase relates to these combined elements.

At the end of the pre-opening phase, however, the excess of demand or offer of securities at prices close to the maximum variation prices, is met by the institutional investors. They send orders that clear the excess of demand or offer connected to the closing of arbitrages positions. This entails a stabilization of the theoretical variation of the pre-opening value of MIB 30 and also increase the volume traded at the opening phase.

A case study may be described as follows: on the eve of the quarterly expiry date of the derivatives a great bunch of index future contract FIB 30 were sold by the market manipulator.

The sale occurs discreetly, in order to avoid a detectable lowering of market quotations.

The sale occurs during a specific short period of time at a precise trading (between 5 and 5.30 p.m.) the day before the expiry. This happens for the following reasons :

- a. market participants cannot mark arbitrage between FIB 30 (the future contract) and the underlying instrument since the cash market is closed,
- b. the manipulator wants to minimize to the over night the risk of the position on the futures sold, since the position is not hedged.

In the first morning of the following day, the suspect manipulator puts huge buy orders on the blue chips composing the index MIB 30 at prices close to the variation prices limits.

These orders are seen by market participants as closing transactions of arbitrage positions or volatility trading.

As a consequence of the high price at which the manipulator is ready to buy the blue chips, the theoretical value of MIB 30 index shows a material increase compared to the last price of the previous day.

During the remaining time of the pre-opening phase (until 9.30 a.m.) institutional investors and the other market participants put sell orders that stabilize the MIB 30 index value.

These investors intend to take advantage of the high value shown by the market, by selling the securities held in their portfolios.

Just before the end of the pre-opening phase the manipulator cancels its buy orders determining an unbalanced situation on the book of the blue chips. The theoretical value of MIB 30 index reacts instantaneously, determining a sudden low variation.

Institutional investors do not have enough time to react and to cancel their sell orders or to insert new buy orders and the market opens low.

It should be noted that the settlement price of FIB 30 at the expiry date, is equal to the value of the opening price of the index MIB 30 on the same date.

The profit realised by the manipulator is equal to the difference between the sale price of FIB 30 contracts sold the day before the eve of the expiry date, and the opening price of the index MIB 30 which the manipulator is able to determine.



## XVII. ANNEX 3 : SUMMARY OF MANIPULATION SUBMISSIONS

### **Submissions from some members of the Emerging Markets Committee Working Group on Enforcement and the Exchange of Information**

#### **I. CYPRUS – Securities and Exchange Commission**

##### A. Conduct Prohibited :

1. It is prohibited for any person to :
  - (a) deceive the public by using dexterous means for the purpose of manipulating prices on the Stock Exchange, or
  - (b) provide information, make statements, promises or predictions which are misleading, fraudulent or false, conceal or withhold material information concerning public listings, or trading in listed stocks.
2. It is prohibited for any person providing information, within the requirements of the Law or the Stock Exchange Regulations, to make a statement which is false, misleading or fraudulent as to any of its material aspects.

##### B. Source of Prohibition :

1. Section 67 of the Cyprus Stock Exchange Law.
2. Section 68 of the Cyprus Stock Exchange Law.

##### C. Standard of Proof :

In both cases, criminal proceedings are subject to the burden of proof, beyond a reasonable doubt, on behalf of the prosecuting authority.

##### D. Other Relevant Authorities :

Criminal Code.

##### E. Available Sanctions :

1. Imprisonment for a maximum term of 7 years or a maximum penalty of up to C£20.000 or both.
2. Imprisonment for a maximum term of 2 years or a maximum penalty of up to C£5.000 or both.

## **II. CZECH REPUBLIC - Czech Securities Commission**

### Conduct Prohibited :

The Securities Act prohibits securities dealers from performing any act aimed at the price manipulation of securities. Any breach thereof constitutes an administrative offence.

The Investment Companies and Investment Funds Act prohibits any person acting in the name of an investment company or an investment fund to manipulate the prices of securities. Any breach thereof constitutes an administrative offence.

There is no specific criminal offence covering manipulation of securities in criminal law. Depending on the scope and nature of the conduct, however, such conduct can be classified as a criminal act and breach of mandatory rules of economic relations, deception or the breach of obligations of a trustee.

### Source of Prohibition :

- Section 47b paragraph 1 letter a) of the Securities Act
- Section 17a paragraph 2 letter b) of the Investment Companies and Investment Funds Act
- Sections 127, 250 or 255 of the Criminal Code

### Standard(s) of Proof :

In criminal proceedings, the conduct and the intention of the suspected person must be proved: “reliable”, “beyond any doubt”, “to the scope necessary”; “material truth must be found”, and “practical certainty must be reached”.

In administrative proceedings before the Securities Commission, similar criteria apply. Guilt (intended or negligent), however, need not be examined, the administrative offence being based on objective responsibility.

**The defending party must prove absence of guilt in regards to the breach of obligations or in the resulting damage. For standards of proof, similar criteria apply as in criminal proceedings.**

### Other Relevant Authorities :

None specified

Available Sanctions :

Imprisonment (up to two years), fines and/or prohibition of further activity may be imposed as a result of criminal proceedings.

Fines and/or prohibition of further activity may be imposed as a result of administrative proceedings.

### **III. HUNGARY – Hungarian Banking and Capital Market Supervision (HBCMS)**

A. Conduct Prohibited :

**The Securities law prohibits price manipulation. Pursuant to the law, the deliberate conduct of any participant of the securities market is classified as unfair price manipulation when:**

- a) withholding information about the securities market,
- b) giving or disclosing unfounded or misleading information,
- c) security movement by one or more persons that are in connection with one another in several transactions, but going in opposite directions,
- d) wash transaction conclusions,
- e) abuse of knowledge involving trading schemes or stock exchange rules of over-the-counter markets; or
- f) disturbing market price movements through any other means, resulting in the development of a price which cannot be properly justified on the basis of information available to the public, and may propel other participants of the market to such conduct which may result in transactions at prices materially different from the real price of the security.

It can also be considered as being unfair price manipulation, when a market participant gives the assignment to display the conduct defined above or otherwise makes others do so.

It shall not be regarded as unfair price manipulation when the issuer, in order to maintain the price of the security it has issued, and/or for the purpose of restoration of the equilibrium in the market, gives an order, in public and in advance - approximately specifying the objective, the quantity and the deadline – for the purchase or sale of the securities it issued and at the end of which, the process discloses the results thereof. Such notice shall be published in a daily paper and in the official gazette of the stock exchange.

It is also stipulated that the investment service provider may not suggest, attempt or conclude a transaction which, owing to its deceptive character, aims at price manipulation resulting in fictitious prices or which are regarded as a disadvantage

to its client. The investment service provider shall also refuse to enter into a contract if it relates to insider trading or is aimed at market manipulation.

B. Source of Prohibition :

Sections 72,73 and 151 of the Hungarian Securities law ( Act No. CXI. of 1996 on the Offering of Securities, Investment Services and on the Stock Exchange).

C. Standard(s) of Proof :

**XVIII. CIVIL PROCEEDINGS: PREPONDERANCE OF THE EVIDENCE**

D. Other Relevant Authorities :

The Hungarian Criminal Code section 299/A on insider trading in securities includes in an implicit manner the notion of price manipulation, but it does not specify it separately.

**Various forms of conduct that could lead to market manipulation are also prohibited under the rules of the Budapest Stock Exchange.**

E. Available sanctions :

Pursuant to the Securities law, the Supervisory Authority is authorised to impose fines in cases, and to the extent stipulated by the law. The amount of the fine is established on the basis of the level of non-compliance with the provisions of the law, separate rules and the resolutions of the Supervisory Authority, as well as to the extent of the financial gain resulting from such non- compliance.

In the case of price manipulation the fine ranges from five hundred thousand to five million Hungarian Forints.  
(As of now, 1USD equals to circa 260HUF)

Note : A proposed comprehensive review of the Securities law is underway. Under the proposed legislative reform it is planned that explicit reference to deliberate conduct (knowingly engaging in the prohibited conduct) is to be removed.

**IV. REPUBLIC OF LATVIA - Securities Market Commission**

A. Conduct Prohibited :

**A. Article 63 of the “Law on Securities”**

1. Participants of the securities market, the manager of the company, his deputies, other officials and employees are forbidden to perform dishonest or manipulative securities transactions, as well as submit false information.
2. Manipulative transactions are such transactions in which securities are bought and sold in order to create the appearance of active trading and thereby encourage other investors to buy or sell the securities. Dishonest transactions are such transactions which do not comply with the general provisions of contract law set forth in Civil Law and which have a detrimental effect on the rights or legal interests of parties to the transaction or other persons.

**B. Article 26, Part 1 of the “Law On Securities”**

No person shall have the right to furnish false information about securities in public offerings and circulation, including information about the sale and purchase of securities.

Source of Prohibition :

Article 63 of the “Law On Securities”  
Article 26, Part 1 of the “Law On Securities”

Standard(s) of Proof :

None specified

Other Relevant Authorities :

None specified

Available Sanctions :

**C. Article 72, Parts 1, 2 and 3 of the “Law On Securities”**

1. If brokers do not observe the provisions of Articles 59, 60, 61, 62 or 63 of this Law, the Commission shall impose upon the broker a fine prescribed in the Latvian Code of Administrative Violations, and may as well revoke the broker’s special permit (license) to conduct activity in the securities market.
2. If a broker fails to observe the requirements laid down in Part 1 of this Article and as a result of that, investors or other persons incur losses, or their rights are violated, the broker shall be held liable under the civil law in accordance with the procedure and in the extent established in legislative acts.
3. If a securities market participant performs transactions referred to in Article 63 of this Law, the Commission shall impose on the guilty person a fine of up to

150% of the profits obtained from the respective transactions or a fine in the amount of up to 200 minimum monthly salaries.

#### **D. Article 69, Part 1 of the “Law On Securities”**

For committing the violations referred to in Article 26 of this Law the Commission may impose on the guilty person a fine in the amount of up to 200 minimum monthly salaries or a fine of up to 150% of the profit made in transactions, if this profit was made as a the result of activities described in Article 26.

- Note 1. Definition of Market participant according Article 1, Part 27 of the “Law On Securities”.  
Participants in the securities market – issuers, investors, brokers, brokerage companies, banks, investment companies, investment consultants and persons putting securities into public circulation.
- Note 2. 200 minimum monthly salaries in Latvia is 10 000 Lats (approximately 17 000 USD).
- Note 3. Latvian Code of Administrative Violations provides sanctions up to 250 Lats (approximately 420 USD).
- Note 4. There are no sanctions for market manipulation in Latvian Criminal Law, but the Securities Market Commission of the Republic of Latvia has now started to work on the materialisation of a market manipulation definition and on amendments to Latvian Criminal Law to determine criminal sanctions for market manipulation.

### **XIX. V. PARAGUAY - COMISIÓN NACIONAL DE VALORES**

#### **B. Conduct Prohibited :**

It is considered illegal conduct to artificially manipulate prices in the securities market, and this conduct is stated in the following articles of Law 1284 of the Securities Market:

Article 165. Functions of the Commission are :

(...)

d) To watch over the correct development of prices in the markets, to which effect the Commission will prescribe rules of general character;

**Article 183. Very severe infractions that affect all the institutions controlled by the Commission are :**

**a) The development of practices directed to falsify the free development of prices in the Securities Market, or that does not implicate the effective**

**transference of property, in contravention to the regulation of the Securities Market.**

(...)

Source of Prohibition :

The Law No. 1284 “on Securities Market”.

Standard(s) of Proof :

None specified

Other Relevant Authorities :

None specified

Available Sanctions :

**Article 194. The faculty to apply the following administrative sanctions will correspond to the Commission :**

- a. Admonition;
- b. Fine up to an amount equivalent to two hundred monthly minimum wages, established for workers of non-specified diverse activities;
- c. Suspension or inability for up to ten years to perform administrative and controlling functions in institutions controlled by the Commission;
- d. Suspension for up to two years of the authorisation to do public offerings of securities;
- e. Prohibition to do public offering of securities; and,
- f. Cancellation of the registration in the Registry that allows the realisation of any of the qualities allowed by this law.

(...)

**Article 228. Will suffer the punishment of prison for one to two years :**

- e. The persons that violate the regulatory provisions of the Securities Market, realise securities transactions with the object of artificially stabilising, setting or varying prices;

## **XX. VI. POLAND – POLISH SECURITIES AND EXCHANGE COMMISSION**

**C. Conduct Prohibited :**

The legal definitions of price manipulation are the following :

1. Criminal liability relating to any person who acting alone or in collusion with others causing an artificial increase or decrease in the price of securities.
2. Criminal liability relating to any person who engages in collusion to the effect of artificially increasing or decreasing the price of securities.

Source of Prohibition :

Article 177 of the Polish Act "The law on the public trading of securities" dated 21 August 1997

Standard(s) of Proof :

Beyond any reasonable doubt.

Other Relevant Authorities :

None specified.

Available Sanctions :

1. Conduct specified above in item A section 1 can lead to a fine of up to 5,000,000 PLZ (approximately 1.25 million USD) and imprisonment for up to 3 years.
2. Conduct specified above in item A section 2 can lead to a fine of up to 5,000,000 PLZ (approximately 1.25 million USD).

## **VII. SOUTH AFRICA - Financial Services Board**

A. Conduct Prohibited :

Section 40 (manipulative practices) of the Stock Exchanges Control Act, 1985 reads as follows :

No person shall :

- (a) by means of any statement, promise, forecast or any other action which he knows to be misleading or which is likely to be misleading induce any other person to buy or sell listed securities; or
- (b) directly or indirectly, whether within or outside a stock exchange, by means of the creation of fictitious transactions or the spreading of false reports attempt to stimulate activities or influence or manipulate the prices of listed securities; or



(c) enter into any transaction, including a bear sale, with the intention of influencing or manipulating the price of listed securities.”

B. Source of Prohibition :

Stock Exchanges Control Act, 1985

C. Standard(s) of Proof :

None specified

D. Other Relevant Authorities :

None specified

E. Available Sanctions :

Any person who contravenes a provision of section 40 shall be guilty of an offence and liable on conviction to a fine or to imprisonment for a period not exceeding five years.

#### **VIII. SRI LANKA - Securities and Exchange Commission of Sri Lanka (SEC)**

A. Conduct Prohibited :

The prohibition relating specifically to securities market manipulation :

The securities law prohibits any person to create, cause to create or do anything that may result in creating a false or misleading appearance or impression of active trading with respect to the market or the price of any securities listed on a stock exchange.

B. Source of Prohibition :

#### **XXI. RULE NO.19 MADE UNDER THE SECURITIES AND EXCHANGE COMMISSION OF SRI LANKA ACT.**

C. Standard of Proof :

Violation of Rule 19 above is Criminal in nature and should be proved in a Court of Law beyond reasonable doubt.

D. Other Relevant Authorities :

**XXII. NONE SPECIFIED****E. Available Sanctions :**

1. Any person found guilty of an offence under the Securities and Exchange Commission Act or any Rules made thereunder shall be liable on conviction after summary trial by a Magistrate, to a sentence of imprisonment of either description for a period not exceeding five years or to a fine not exceeding ten million rupees or to both such imprisonment and fine.
2. The Commission (SEC), having regard to the circumstances in which the offence under this Act was committed, may compound such offence for a sum of money not exceeding one third of the maximum fine impassable for such offence and all such sums of money received by the Commission in the compounding of an offence under this section, shall be credited to the compensation fund.
3. The Commission shall cancel or suspend licenses granted to a stockbroker or a stock dealer, where the Commission is satisfied that: the stock broker or the stock dealer has acted in breach of any provisions of this Act, or any Rules or Regulations made under the Act; or -the stockbroker or the stock dealer is guilty of malpractice or irregularity in the management of his affairs.

**XXIII. IX. THAILAND -- THE OFFICE OF THE SECURITIES AND EXCHANGE COMMISSION****A. Conduct Prohibited :**

1. Washed sale
2. Matched order
3. Series of transactions to induce others to purchase or sell listed securities
4. Other types of false or fictitious trades

**B. Source of Prohibition :****A.****B. Securities and Exchange Act B.E. 2535 (A.D. 1992) (the SEC Act)****C. Standard(s) of Proof :**

Beyond reasonable doubt. (criminal offence)

**D. Other Relevant Authorities :**

## C.

- D. 1. The Royal Thai Police Headquarters
- E. 2. The Office of the Attorney General

## E. Available Sanctions :

- 1. **Criminal sanctions : Imprisonment not exceeding 2 years and/or a fine not exceeding 2 times the benefit received or which should have been received as a result of contravention but such a fine shall be no less than Baht 500,000. (approximately Baht 38 = US\$ 1)**

2. **Administrative sanctions :**

2.1 If an offender is the manager of a securities company, fund manager, property valuer, auditor or financial advisor approved by the Office of the SEC (the Office), the Office shall consider that such person does not meet qualifications or has prohibitive characteristics and therefore shall be temporarily suspended or permanently withdrawn from approval depending on the severity of each case.

2.2 If an offender is the person who is going to apply for the Office's approval for being the manager of a securities company, fund manager, property valuer, auditor or financial advisor, the Office shall consider that such person has prohibitive characteristics and shall not grant approval to such person. However, the prohibition period will be determined on a case by case basis depending on severity.

2.3 If an offender is the manager of a company that applies for the Office's approval for public offering, the Office will consider qualifications of the management of such company as one of the key factors in considering granting approval to such a company.

- 3. **Public reprimand : Information on offender's wrongdoing will be disclosed to the public.**

## F.

G. X. TURKEY - Capital Market Board

## A. Conduct Prohibited :

- 1) Real entities, the authorised persons of legal entities and those acting together with them dealing with trading in capital market instruments in order to artificially affect their demand and supply and to give the

impression of the existence of an active market for which they hold prices at the same level and increase or decrease the prices.

- 2) Real entities, the authorised persons of legal entities and those acting together with them who give and disseminate misleading, false, deceiving information and news, make comments or do not disclose the information to be disclosed.

B. Source of Prohibition :

**Capital Market Law , Section V, Article 47(A)/1-2**

C. Standard(s) of Proof :

It is subject to criminal prosecution. Therefore, knowingly engagement and specific intent (motive) should be proved beyond reasonable doubt.

D. Other Relevant Authorities :

None specified

E. Available Sanctions :

- Imprisonment from 2 years to 5 years and a heavy fine from TL 10 billion (about 20.000 USD) to TL 25 billion ( about 50.000 USD) ; heavy fines have to be at least three-times the benefit obtained through the offence committed, being independent on any upper level
- In the case of the repetition of these acts, the penalties given shall then be increased by one half.
- The Capital Market Board has the authority to take necessary measures in order to prevent those involved in any market manipulation activity to trade in any organised and regulated securities market.

Note : Market intermediaries licensed by The Capital Market Board are prohibited to engage or to aid any manipulative conduct according to the rules about intermediary activities released by the Board and the Istanbul Stock Exchange. Any violation of these Rules is subject to an administrative fine up to or equivalent to 50.000 USD by the Board and disciplinary action ranging from temporary to permanent suspension of brokerage activities in the stock exchange by the ISE.