

Fair market conduct: Typology, problems and policy

Bhargavi Zaveri

Finance Research Group, IGIDR

October 11, 2017

Concept of market conduct

Market conduct considers how persons involved in the financial sector conduct themselves and their businesses in relation to clients, customers, and each other, with a focus on fairness and integrity. (*Draft market conduct policy for South Africa (2014)*)

Concept of market conduct

Market conduct considers how persons involved in the financial sector conduct themselves and their businesses in relation to clients, customers, and each other, with a focus on fairness and integrity. (*Draft market conduct policy for South Africa (2014)*)

1. Consumer protection: Conduct between financial firms and consumers.
2. Market abuse: Conduct between financial firms when trading on a market.

Market abuse: Conceptual framework

Market abuse: Enforcement framework

Market abuse enforcement: State of play

Thoughts for the panel

Market abuse: Economics v. Law

Market abuse: Economics v. Law

Economics

- Information asymmetry
- Market power
- Public goods
- Externalities

Market abuse: Economics v. Law

Economics

- Information asymmetry
- Market power
- Public goods
- Externalities

Law

- manipulative or deceptive
- defraud
- practice that operates as a fraud or deceit
- trading when in possession of UPSI

Fraud: Common law v. SEBI

Common law

- Misrepresentation of fact
- Intention
- Materiality
- Reliance on the fraud
- Actual resulting loss

Fraud: Common law v. SEBI

Common law

- Misrepresentation of fact
- Intention
- Materiality
- Reliance on the fraud
- Actual resulting loss

SEBI

- act, omission or concealment
- whether in a deceitful manner or not
- to induce another person to deal in securities
- whether or not there is any wrongful gain or avoidance of loss

SEBI's definition of fraud: Problems

Missing elements in SEBI's definition of "fraud":

1. specifically does away with deceit
2. no materiality required
3. no reliance on the fraud
4. specifically does away with actual resulting loss.

SEBI's definition of fraud: Problems

Missing elements in SEBI's definition of "fraud":

1. specifically does away with deceit
2. no materiality required
3. no reliance on the fraud
4. specifically does away with actual resulting loss.

Always arguable that it is enforced differently!

How does the world define market abuse?

EU Market Abuse Regulation (2014): *“Market abuse is a concept that encompasses unlawful behaviour in the financial markets and, for the purposes of this Regulation, it should be understood to consist of insider dealing, unlawful disclosure of inside information and market manipulation. Such behaviour prevents full and proper market transparency, which is a prerequisite for trading for all economic actors in integrated financial markets.”*

How does the world define market abuse?

EU Market Abuse Regulation (2014): *“Market abuse is a concept that encompasses unlawful behaviour in the financial markets and, for the purposes of this Regulation, it should be understood to consist of insider dealing, unlawful disclosure of inside information and market manipulation. Such behaviour prevents full and proper market transparency, which is a prerequisite for trading for all economic actors in integrated financial markets.”*

FSMA (2000): *“Market abuse is behaviour which falls within any one or more of the types of behaviour set out in sub-sections (2) to (8) of the Act.”*

How does the world define market abuse?

EU Market Abuse Regulation (2014): *“Market abuse is a concept that encompasses unlawful behaviour in the financial markets and, for the purposes of this Regulation, it should be understood to consist of insider dealing, unlawful disclosure of inside information and market manipulation. Such behaviour prevents full and proper market transparency, which is a prerequisite for trading for all economic actors in integrated financial markets.”*

FSMA (2000): *“Market abuse is behaviour which falls within any one or more of the types of behaviour set out in sub-sections (2) to (8) of the Act.”*

Securities Exchange Act (1934): Does not define market abuse, but prohibits a list of activities categorized as market manipulation.

Note: Finite list of conduct amount to market abuse.

SEBI's power to punish and prevent market abuse

Issue directions under S.11B:

- in the interest of investors, or orderly development of securities market;
- to prevent the affairs of any intermediary being conducted in a manner detrimental to the interest of investors or securities market;
or
- to secure the proper management of any such intermediary or person.

SEBI's power to punish and prevent market abuse

Issue directions under S.11B:

- in the interest of investors, or orderly development of securities market;
- to prevent the affairs of any intermediary being conducted in a manner detrimental to the interest of investors or securities market;
or
- to secure the proper management of any such intermediary or person.

TO

- any intermediary or class of intermediary, or
- any person associated with the securities market; or
- any company proposed to be listed, as may be appropriate in the interests of investors in securities and the securities market.

SEBI's power to prevent and punish market abuse (contd.)

Directions pending investigation or on completion of investigation under Section 11(4):

1. suspend trading of any security;
2. restrain access to the securities market;
3. suspend any office-bearer of any exchange or self-regulatory organisation from holding such position;
4. impound and retain the proceeds or securities in respect of any transaction which is under investigation;
5. attach, for not more than 1 month, bank accounts of any intermediary or any person associated with the securities market in any manner involved in violation of any of the provisions of this Act;
6. direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction under investigation

Opportunity of being heard may be given before or after passing such orders

Scope of data set

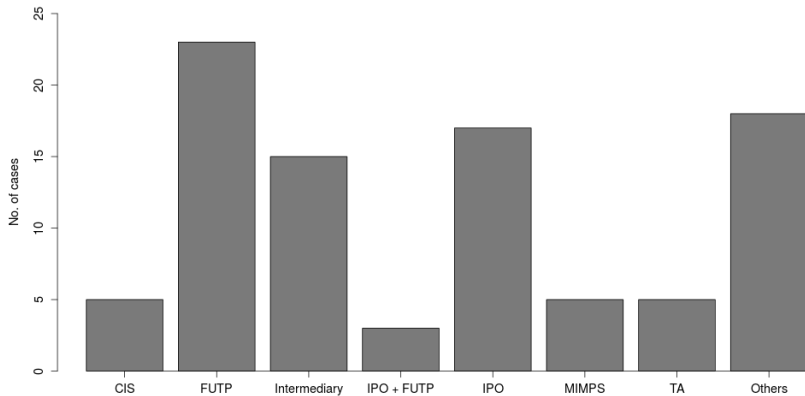
- Study period: January 1, 2008 - April 30, 2016.
- Total number of final orders passed by the WTM: 2278.
- Number of orders studied: 91.
 - No. of interim orders: 16
 - No. of final orders: 75
- Source of data: Website of the SEBI.¹

¹Data-set built by researchers at NIPFP, New Delhi. Summary compiled by Surbhi Bhatia at the Finance Research Group, IGIDR.

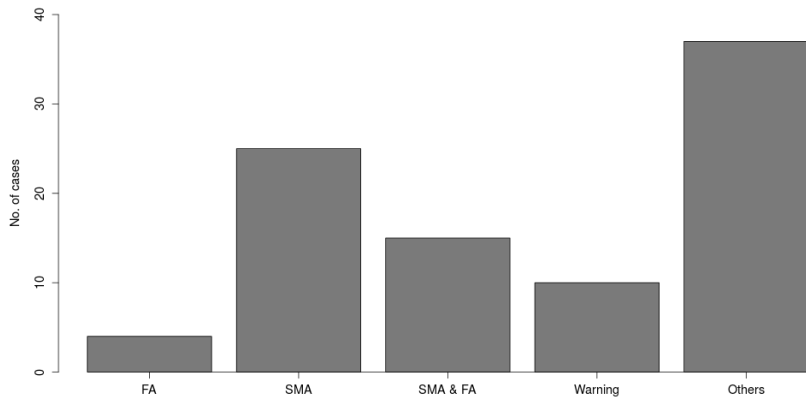
Fields captured

- Name of the order.
- Date of violation.
- Date of order.
- Ex-parte or not.
- Type of violation.
- Amount involved in the violation.
- Punishment.
- Duration for which the punishment should operate.

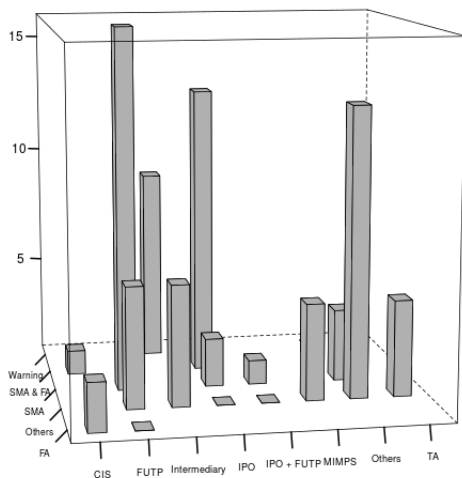
What kind of violations triggered the “11s”?



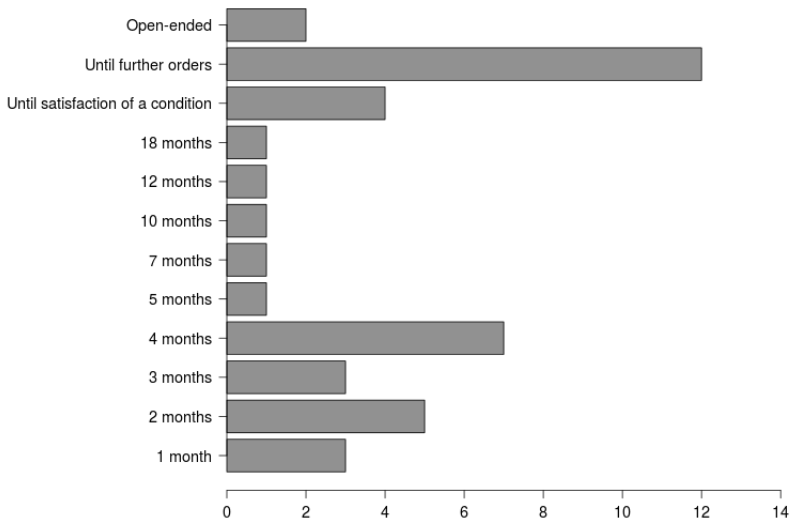
What kind of directions were issued under the “11s”?



Directions issued for different kinds of violations



Duration of directions



Time for disposal of cases

No. of observations = 68

	In months
Range	1-190
Average	68
1st quartile	29.75
Median	63
3rd quartile	98.75

Closing thoughts

1. Scope of FUTP Regulations:
 - Consumer protection and market abuse require differently designed policy interventions
2. Definitional issues:
 - Economic ideas of market abuse to be imported into the law
 - Idea of fraud must be re-visited.
3. Defining enforcement powers better...and sharper.