

A Rapid Response to Questionable Trading – moving towards better enforcement of Australia’s securities laws

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The global financial crisis has acutely exposed the global nature of the markets for securities and their impact on the world economy. Yet despite some cross-fertilization, the regulation of those markets differs significantly. In the longer term it is likely that governments will now move towards the setting of more uniform securities laws and a more coordinated response to their enforcement. However in the short term can more be done to ensure that the Australian Securities and Investments Commission (ASIC) and the Australian Stock Exchange (ASX) improve their enforcement of Australia’s securities laws, in particular the prohibitions against insider trading and market manipulation? ASIC has recently undertaken a review of its structure in an effort to become more market focused. The ASX has established a separate company to undertake supervision of its markets. However both ASIC and the ASX operate under existing laws and procedures that divide the supervision of regulating the markets between them. This article will consider whether changes are needed to both their enforcement tools and this division of regulation to prompt a quicker enforcement response and to respond to the challenges of a likely move towards worldwide harmonization of securities regulation.

Introduction

It is an understatement to observe that recent events have put the spotlight on stock markets worldwide. Wild swings of share price indices have been given front page newspaper coverage. Tales of market misconduct have been circulating in the media¹ and there has been an increase in complaints of market abuse to regulators.² Confidence in the stock markets is probably at its lowest level in most peoples’ memory.

It may take a long time, perhaps many years, for confidence in stock markets to be restored, particularly for retail ‘mum and dad’ type investors. Now, more than ever, it seems critical that the market regulators increase their efforts in enforcing legislation that prohibits market misconduct in order to help to restore confidence in the markets. Retail investors are unlikely to wade back in to the market until they are confident that the

¹ See for example I Verreter “Small investors bear the brunt of information vacuum” The Sydney Morning Herald, 21 February 2008 at 25; S Washington “Open the books” The Sydney Morning Herald, 23 February 2008 at 3; J Whyte “Unlucky Broker Caught in Rumourage”, Australian Financial Review, 13 March 2008 at 32 and E Knight “Investment banking’s big guns fall into rumourage trap”, The Sydney Morning Herald, 19 September 2008 at 19.

² See for example comments by B Gibson - Commissioner ASIC, that “There has been a marked increase in complaints about illegal market conduct – insider trading, market manipulation, late disclosure of information to the market and the spreading of false rumours “ ‘Lessons Learnt from market volatility and sub-prime’ address to the Innovate O8 IFSA Conference 7 August 2008 at 7, [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Gibson_market_turmoil_response_Aug_08.pdf/\\$file/Gibson_market_turmoil_response_Aug_08.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Gibson_market_turmoil_response_Aug_08.pdf/$file/Gibson_market_turmoil_response_Aug_08.pdf) viewed 12 December 2008.

market is a level playing field that does not unfairly advantage those in the securities industry.

This article considers what changes could be made relatively quickly to improve enforcement of Australia's securities laws which prohibit market misconduct. In Part I the roles of both the ASX and ASIC to take action against market abuse is outlined together with their investigative powers and methods. In Part II the enforcement record of ASIC taking action is examined, particularly in relation to matters where the ASX detected a possible contravention. In Part III consideration is given to whether there should be a strengthening in the powers of ASIC and the ASX and what form these additional powers might take. In Part IV the current division of market supervision between ASX and ASIC is considered to ascertain whether this could be arranged differently with a view to more effectively enforcing the market misconduct provisions.

I The Enforcement Roles and Powers of the ASX and the ASIC

In Australia, like many countries around the world, the power to take action for stock market misconduct is split between the government regulator, ASIC, and a self regulatory organization, the ASX.³

The Enforcement role of the Australian Securities and Investments Commission

ASIC is the Australian Government's regulator of markets. It is responsible for, inter alia, enforcing the *Corporations Act 2001* (Cth) (Corporations Act). Part 7.10 of the Corporations Act contains the provisions in relation to market misconduct which include the prohibitions against:

- market manipulation;⁴
- making false statements and disseminating false information;⁵
- insider trading;⁶ and
- engaging in dishonest conduct.⁷

The prohibition against dishonest conduct is very broad and would catch behaviour that may fall outside one of the more specific provisions. It provides:

A person must not, in the course of carrying on a financial services business in this jurisdiction, engage in dishonest conduct in relation to a financial product or financial service.⁸

³ For a consideration of the split between the enforcement roles in France, Japan, Germany, the United Kingdom, Hong Kong, the United States and Canada see S Gadinis and H E Jackson "Markets as Regulators; A Survey" June 2007, <http://ssrn.com/abstract=960168>.

⁴ *Corporations Act 2001* (Cth) ss 1041A-1041C.

⁵ *Corporations Act 2001* (Cth) ss 1041D-1041F.

⁶ *Corporations Act 2001* (Cth) s 1043A.

⁷ *Corporations Act 2001* (Cth) s 1041G. For a discussion as to the meaning of dishonesty under this section see J Austin "Is my client's conduct Dishonest or merely excusable sharp practice" Third International Legal Ethics Conference, Gold Coast, 14 July 2008, <http://ssrn.com/abstract=1288970>.

⁸ *Corporations Act 2001* (Cth) s 1041G.

ASIC may seek a wide range of remedies in relation to a breach of these provisions. For example, ASIC can seek freezing orders or injunctions from the court under ss 1323 and 1324 of the Corporations Act and/or orders pursuant to s 1325 that compensation be paid to any victims. The dishonest conduct prohibition is a criminal offence which has a maximum penalty of a fine of \$22,000 and/or imprisonment for 5 years.⁹ Similarly the prohibitions against market manipulation, insider trading, and making false statements and disseminating false information are also all criminal offences carrying the same penalty, with the exception of insider trading where the maximum fine is \$220,000.¹⁰ Alternatively, or in addition to, except in the case of the dishonest conduct offence, ASIC can bring civil penalty proceedings seeking civil penalties of up to \$200,000 for an individual and \$1 million for a corporation, compensation for any victims and/or orders disqualifying the perpetrators from being involved in the management of corporations.¹¹

ASIC – Detection and Investigation

ASIC detects market abuse from surveillance it undertakes, complaints from the public, referrals from other agencies (such as the ASX) and the media.¹²

Pursuant to s.13 of the *Australian Securities and Investments Commission Act 2001* (Cth) (ASIC Act), if it has reason to suspect a contravention of Corporations Act, it can commence an investigation. In conducting such investigation, like other law enforcement agencies such as the State, Territory and Federal Police, ASIC takes statements and gathers evidence from witnesses. However, unlike some other law enforcement agencies, ASIC has some additional investigation powers contained in Part 3 of the ASIC Act. ASIC has the power to issue notices to inspect or produce documents¹³ and to compel a person to appear before it and answer questions.¹⁴ In addition ASIC can require a person to give it reasonable assistance in connection with an investigation and any subsequent prosecution.¹⁵ The rationale for a body such as ASIC to be vested with these additional powers, not available to the State, Territory and Federal Police, is the complexity of the commercial crimes it is charged to investigate.¹⁶

⁹ *Corporations Act 2001* (Cth) s 1041G, s 1311. As to the definition of “penalty unit” see *Crimes Act 1914* (Cth) s 4AA.

¹⁰ *Corporations Act 2001* (Cth) s 1311. As to the definition of “penalty unit” see *Crimes Act 1914* (Cth) s 4AA.

¹¹ *Corporations Act 2001* (Cth) ss 1317E – 1317HA, s 206C. Note criminal proceedings may be brought after proceedings for a civil penalty for the same conduct but if a person has been convicted of the criminal offence civil penalty proceedings cannot be brought: see ss 1317N-1317P.

¹² “ASIC: a guide to how we work” at 10

[http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/asic_guide_how_we_work.pdf/\\$file/asic_guide_how_we_work.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/asic_guide_how_we_work.pdf/$file/asic_guide_how_we_work.pdf) viewed 12 December 2008.

¹³ *Australian Securities and Investments Commission Act 2001* ss 29- 34.

¹⁴ *Australian Securities and Investments Commission Act 2001* s 19.

¹⁵ *Australian Securities and Investments Commission Act 2001* s 19(2)(a) and s 49.

¹⁶ See generally J P Longo “The Powers of Investigations of The Australian Securities Commission: Balancing the Interests of Persons and Companies under Investigation with the Interests of the State” (1992) 10 (4) CSLJ 237.

The Enforcement Role of the Australian Stock Exchange Limited

The ASX is a self regulatory organization. It was formed in 1987 when the six independent stock exchanges that formerly operated in the state capital cities were amalgamated.¹⁷ In 1998 the ASX was demutualised and became a public company incorporated under the Corporations Act with its shares listed on the exchange that it operates.¹⁸ The ASX holds a licence under s 795B of the Corporations Act to operate the Australian Stock Exchange.¹⁹ Under the terms of its licence it is required to, inter alia, “do all things necessary to ensure that the market is fair, orderly and transparent” and to have adequate arrangements for supervising the market including arrangements to monitor the conduct of participants and to enforce compliance with the market’s operating rules.²⁰ It is also required to give reasonable assistance to ASIC²¹ and provide ASIC with written notice as soon as practicable if it has “reason to suspect that a person has committed, is committing, or is about to commit a significant contravention” of the Corporations Act, detailing the persons name, the contravention and the reasons ASX believes there has or will be a contravention.²²

In addition, as a market licensee, the ASX it is required to maintain operating rules dealing with matters prescribed in the regulations.²³ As part of its operating rules, the ASX has prescribed ‘Market Rules’ which contain rules in relation to how a person, called a ‘participant’, can gain access to trade or execute orders on the Australian Stock Exchange and the on-going obligations of participants.²⁴ Pursuant to s 793C of the Corporations Act these rules have effect as a contract between the ASX and each of the participants in the market and between a participant and each other participant.

Included in the obligations of participants contained within the Market Rules are that participants and executives of market participants must not engage in market manipulation or unprofessional conduct.²⁵ “Unprofessional conduct” is defined in Market Rule 2.10 to include:

- (a) conduct which amounts to impropriety affecting professional character and which is indicative of a failure either to understand or to practise the precepts of honesty or fair dealing in relation to other Market Participants, clients or the public;
- (b) unsatisfactory professional conduct, where the conduct involves a substantial or consistent failure to reach reasonable standards of competence and diligence;and

¹⁷ See “History of the market”, <http://www.asx.com.au/about/asx/history/index.htm> viewed 12 December 2008.

¹⁸ Robert Baxt, A. B., Pamela Hanrahan (2008) *Securities and Financial Services Law*. LexisNexis Butterworths, Australia, 2008, at 382.

¹⁹ See “ASX’s regulatory licences”, http://www.asx.com.au/supervision/supervisory_role/regulatory_licenses.htm viewed 12 December 2008.

²⁰ *Corporations Act 2001* (Cth) s 792A.

²¹ *Corporations Act 2001* (Cth) s 792D.

²² *Corporations Act 2001* (Cth) s 792B.

²³ *Corporations Act 2001* (Cth) s. 793A.

²⁴ See generally “A Guide to becoming an ASX Market Participant”, https://www.asxonline.com/intradoc-cgi/groups/participant_services/documents/information/asx013012.pdf viewed 12 December 2008.

²⁵ See *ASX Market Rules* 13.4-13.5 and 28.3.1, http://www.asx.com.au/supervision/rules_guidance/market_rules.htm viewed 12 December 2008.

- (c) conduct which is, or could reasonable be considered as likely to be, prejudicial to the interests of ASX or its Market Participants.

If a market participant or an executive of a market participant breaches the Market Rules or engages in unprofessional conduct the ASX may take disciplinary action.²⁶ In effect this means that the matter will be referred to the ASX Disciplinary Tribunal.²⁷ This Tribunal has broad powers to censure, impose a fine of up to \$1 million, suspend the market participant or terminate its admission to the ASX.²⁸

Obviously a clear limitation on ASX's powers is that it can only sanction market participants, that is, stockbrokers and their executives, for a breach of its rules. The ASX has no powers to take action against others, such as clients of stockbrokers, who engage in market misconduct. This limitation is particularly significant given the increase in recent years of brokers allowing 'straight through' processing of buy and sell orders via the internet without the client having to speak to a broker. Although Market Rules 13.3.1-13.3.2 requires that brokers offering straight through order processing have procedures in place to prevent manipulative trading,²⁹ instances of market manipulation via trading through such brokers appears to be on the increase relative to trading through traditional 'advisory' brokers.³⁰

ASX Detection and Investigation

Since 1 July 2006 ASX detection and investigation functions have been vested in ASX Markets Supervision Pty Limited [ASXMS]. ASXMS is a separate company to the ASX although it is a wholly owned subsidiary of the ASX and is funded by the ASX.³¹ It is governed by a board comprising 5 directors, 3 of whom are also ASX directors and 2 of whom are independent directors.³²

Pursuant to Market Rule 28, the ASX has broad powers to investigate possible breaches of its rules. These powers include the power to require production of documents and

²⁶ See *ASX Market Rules* 28.3.1 http://www.asx.com.au/supervision/rules_guidance/market_rules.htm viewed 12 December 2008.

²⁷ See *ASX Disciplinary Processes and Appeals Rulebook*, http://www.asx.com.au/supervision/rules_guidance/disciplinary_rules.htm viewed 12 December 2008.

²⁸ *Ibid.*

²⁹ See generally *Automated Order Processing: Operational Requirements* ASX Market Rules Guidance Note 22 http://www.asx.com.au/supervision/rules_guidance/asx/asx_gn22_automated_order_processing_operatioal_requirements.pdf viewed 12 December 2008.

³⁰ J Rydge and C Comerton-Forde "The Importance of Market Integrity, An Analysis of ASX Regulation" 1 September 2004 SIRCA Research, http://www.asx.com.au/about/pdf/The_Importance_of_Market_Integrity_-_September_2004.pdf viewed 12 December 2008.

³¹ *Australian Stock Exchange 2008 Annual Report* at 109, http://www.asx.com.au/about/pdf/annual_report_2008.pdf, viewed 12 December 2008.

³² Mayne, E. "ASX Markets Supervision - 'Looking Forward', SDIA Conference, Sydney, 1 June 2007 at p.2, http://www.asx.com.au/supervision/pdf/sdia_conference_speech_david_lawrence_june07.pdf viewed 12 December 2008.

inspect the premises of market participants.³³ In addition the ASX can require market participants and their employees to attend an interview and give it any information it requires.³⁴

ASXMS principle method of detecting market abuse is via surveillance it conducts using its SMARTS (Securities Market Automated Research Trading and Surveillance) computer system. This monitors all real-time trading information and highlights any unusual price or volume movements and triggers an alert. The process after an alert is as follows:

Each alert is referred to an analyst, who assesses the market conditions that caused it. For example, the analyst might determine that public information such as a report on the stock by a stockbroker, a company announcement or newspaper report or broader market conditions (such as commodity prices) can explain the market activity. Surveillance analysts also look for patterns of alerts, which may indicate that an attempt is being made to interfere with normal market forces, requiring further investigation.³⁵

ASX referral of matters to ASIC

When suspicious trading has been detected the ASX is required to refer this to ASIC pursuant to the terms of its licence and its memorandum of understanding with ASIC.³⁶ Prior to sending the referral the ASX conducts its own investigation described as follows:

Prior to any referral to ASIC we undertake considerable analysis of trading data, broker records and other available information to determine whether or not there is prima facie evidence of insider trading. A referral to ASIC will include a detailed report comprising chronology, analysis, all relevant data and identification of those people who may be of most interest should ASIC pursue further investigations.³⁷

ASIC has stated that the procedure from this point on is that the ASX referrals go to a 'Market Watch' team in ASIC for a preliminary assessment. If the Market Watch team decides there is substance to the referral then it is passed on to the 'Enforcement' team. It is the job of the Enforcement team to gather admissible evidence so that ASIC is in a position to commence legal proceedings.³⁸

³³ See *ASX Market Rules* 28.1.1, http://www.asx.com.au/supervision/rules_guidance/market_rules.htm viewed 12 December 2008.

³⁴ See *ASX Market Rules* 28.1.3, http://www.asx.com.au/supervision/rules_guidance/market_rules.htm viewed 12 December 2008

³⁵ See "SMARTS", <http://www.asx.com.au/supervision/participants/smarts.htm> viewed 12 December 2008.

³⁶ *Memorandum of Understanding between Australian Securities and Investments Commission and Australian Stock Exchange Limited*, 30 June 2004, <http://www.asx.com.au/about/pdf/ASICMOU.pdf> viewed 12 December 2008.

³⁷ Lawrence, D. "ASX Markets Supervision" 11th Annual SDIA Conference, 22 May 2008, http://www.asx.com.au/supervision/pdf/sdia_speech_melb_may08_mayne_lawrence.pdf viewed 12 December 2008.

³⁸ B Gibson, "Improving confidence and integrity in Australia's capital markets", Presentation to the Committee for Economic Development of Australia, Sydney, 8 July 2008 [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Gibson_26-3-08_asx_seminar.pdf/\\$file/Gibson_26-3-08_asx_seminar.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Gibson_26-3-08_asx_seminar.pdf/$file/Gibson_26-3-08_asx_seminar.pdf) viewed 12 December 2008.

II The Enforcement Record of the ASX and ASIC

As is outlined above ASX and ASIC can resort to significant sanctions in dealing with market abuse. Yet despite this, the number of matters in relation to which ASIC has taken action to enforce securities laws remains low, particularly for matters where the ASX detected a possible contravention and referred it to ASIC.

Set out in Annexure A is a table compiled from ASIC media releases and the annual reports of ASIC and the ASX showing successful and unsuccessful actions taken by ASIC as a result of ASX referrals in the last 10 years. In most years only a handful of ASX referrals result in enforcement action by ASIC and even fewer were successful. Whilst the ASX has successfully increased its disciplinary action against participants in its market over the last 10 years, including for market manipulation,³⁹ it has not been able to translate this success into ASIC successfully bringing action as a result of ASX referrals.

This low rate of success by ASX must surely be a source of frustration for the ASX given the relatively high level of resources it commits to market supervision.⁴⁰ It is perhaps not surprising then that the new Chairman of ASIC, Tony D'Aloisio (formally the CEO of the ASX) has said that one of ASIC's main priorities going forward is to "stamp out insider trading and market manipulation and to improve disclosure."⁴¹ As such he has directed more of ASIC's resources to enforcement in this area including the creation of a special task force to determine what additional actions ASIC can take to improve disclosure and fight insider trading and market manipulation.⁴² This is also partly a response to a recent survey conducted by ASIC in which the businesses surveyed wanted prosecuting market abuses, such as insider trading and market manipulation, to be a priority for ASIC.⁴³

³⁹ See *Australian Stock Exchange 2008 Annual Report* at 29-30, http://www.asx.com.au/about/pdf/annual_report_2008.pdf viewed 12 December 2008, which reported that in 2008 the number of matters finalized by the Disciplinary Tribunal increased to 28 compared to 24 in 2007 generating fines of \$1.1M, 137% higher than 2007 including a \$175,000 fine for market manipulation. Although it should be noted that the maximum penalty the Disciplinary Tribunal could impose increased to \$1M during 2008 which may be responsible, in part, for the increase in fines imposed.

⁴⁰ See E Mayne, Chief Supervision Officer, ASX "Private Equity Australia: ASX's Key Regulatory Principles – 18 March 2008" at 12 http://www.asx.com.au/supervision/pdf/brw_private_equity_18_march_08.pdf viewed 12 December 2008 in which he states that from 2007 to 2008 the number of employees involved in supervision is 105 having increased from 84 in 2006.

⁴¹ T D'Aloisio "Securities markets, participants and ASIC" Securities & Derivatives Industry Association Conference, Melbourne, 22 May 2008 at 3 [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Securities%20markets.%20participants%20and%20ASIC.pdf/\\$file/Securities%20markets.%20participants%20and%20ASIC.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Securities%20markets.%20participants%20and%20ASIC.pdf/$file/Securities%20markets.%20participants%20and%20ASIC.pdf) viewed 12 December 2008.

⁴² *Ibid* at 5 and 19.

⁴³ See The Allen Consulting Group *ASIC Stakeholder Survey*, April 2008 at 8 [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Stakeholder_survey_2008.pdf/\\$file/Stakeholder_survey_2008.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Stakeholder_survey_2008.pdf/$file/Stakeholder_survey_2008.pdf), viewed 16 December 2008.

Measuring ASIC/ASX Enforcement

The main challenge in trying to judge whether or not ASIC and the ASX are successful in their enforcement efforts is that it is difficult, if not impossible, to ascertain the level of market abuse that actually takes place. Given the focus by ASIC's Chairman to this issue he, at least, believes that market manipulation and insider trading is still a problem for Australia's markets.

It appears that insider trading is more prevalent in bull markets such as the one which ended recently on the basis that insider trading tends to occur around takeovers, profit announcements and profit warnings.⁴⁴ In the UK a recent study by the Financial Services Authority found that a significant number of takeover announcements were preceded by abnormal trading volumes immediately prior to the announcement, suggesting insider trading.⁴⁵ Similar studies in the US and Canada have shown similar abnormal price movements shortly prior to mergers, takeovers and earnings announcements.⁴⁶

Regrettably, there have been no recent similar studies conducted on Australia's markets⁴⁷ although anecdotally at least, market participants have observed similar movements prior to takeovers and mergers.⁴⁸ There are also sound arguments why it could be expected that insider trading is increasing:

The arguments in favour of insider trading getting worse are, firstly, the greater sophistication of markets, which has led to more instruments and greater ability to arbitrage between markets. Secondly, it's greater market liquidity – an easier ability to hide insider trading. Thirdly, it's the greater importance, the much greater importance, of trading to investment banks – remuneration structures within investment banks and broking firms which encourage short-termism because of the annual bonus cycle and the global pervasiveness and complexity of financial institutions.⁴⁹

In addition, the relatively recent proliferation of highly geared hedge funds with remuneration structures designed to provide massive rewards for performance also

⁴⁴Lawrence D “ASX Markets Supervision” 11th Annual SDIA Conference, 22 May 2008 at 8 http://www.asx.com.au/supervision/pdf/sdia_speech_melb_may08_mayne_lawrence.pdf viewed 12 December 2008

⁴⁵ N Monteiro, Q Zaman and S Leitterstorf “Updated Measure of Market Cleanliness” Financial Services Authority Occasional Paper 25 <http://www.fsa.gov.uk/pubs/occpapers/op25.pdf>, viewed 12 December 2008.

⁴⁶ For a summary of such studies see “Testimony of James D. Cox before Committee on the Judiciary United States Senate September 26, 2006 on Insider Trading” <http://www.law.duke.edu/features/pdf/coxjudiciaryintradetestimony.pdf> viewed 12 December 2008.

⁴⁷ There were some empirical studies conducted between 1998 and 2002. For a summary of these see G Lyon and JJ du Plessis *The Law of Insider Trading in Australia*, The Federation Press, Sydney, 2005 at 161-163.

⁴⁸ See comments by P Hunt “Insider trading on the rise-perception or reality?” ASIC Summer School 2008, Sydney, Panel Discussion at 77, [http://www.fido.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/Australias_capital_markets.pdf/\\$file/Australia_capital_markets.pdf](http://www.fido.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/Australias_capital_markets.pdf/$file/Australia_capital_markets.pdf).

⁴⁹ Ibid at 78.

support the suspicion that there may be an increase in market misconduct, such as insider trading, by such funds.⁵⁰

In bear markets, such as that being experienced at present, there may be more instances of market manipulation as attempts are made to ‘prop up’ prices when markets are declining. In May 2008 the ASX has noted that it had detected the beginning of this as a trend:

We have seen an increase in apparent instances of price support by clients of brokers. This invariably in thinly traded stocks whose price is under pressure. There may be any number of motives for this including the avoidance of margin calls – whether they be calls of directors or just shareholders. While the incidence is not “rampant” or significant, it is an embryonic trend and it tends to be clients, not brokers.⁵¹

Declining remuneration of brokers and others in a bear market may also trigger breaches of securities laws in an effort to maintain lifestyle and meet commitments:

These risks may manifest themselves as excessive transactions; churning; unauthorized activity; interception of confirmations or monthly statements; fraud; diversion of client monies etc.⁵²

Although it is difficult to determine what level of market abuse still exists in the market the references and arguments listed above tend to suggest that there is still some abuse and that this may be on the increase. Perhaps what is of more concern is that even when the ASX detects possible abuse and refers a matter to ASIC it often seems that it does not proceed to successful enforcement action being taken or ASIC taking any action at all.

This is of concern given the resources the ASX commits to surveillance and that the enforcement of securities laws is critical to market integrity. A number of studies have shown that effective enforcement of securities laws is fundamental to market integrity and that markets which lack integrity have a higher cost of capital for their participants.⁵³ A lack of market integrity reduces investor confidence in the market, investors being wary of investing in a market which is not considered fair for all participants or where investors may lose their investment to unscrupulous operators. Effective enforcement

⁵⁰ T D'Aloisio, ASIC Chairman, (2008), “Securities markets, participants and the ASIC”, Securities & Derivatives Industry Association Conference. Melbourne, 22 May 2008 at 19 [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Securities%20markets.%20participants%20and%20ASIC.pdf/\\$file/Securities%20markets.%20participants%20and%20ASIC.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Securities%20markets.%20participants%20and%20ASIC.pdf/$file/Securities%20markets.%20participants%20and%20ASIC.pdf) viewed 12 December 2008.

⁵¹ Lawrence D “ASX Markets Supervision” 11th Annual SDIA Conference 22 May 2008 at 9 http://www.asx.com.au/supervision/pdf/sdia_speech_melb_may08_mayne_lawrence.pdf viewed 12 December 2008.

⁵² Ibid at 10.

⁵³ See for example Bhattacharya, U. and H. Daouk, 2002, “The World Price of Insider Trading”, Journal of Finance 57 and Hail, L. and C. Leuz, 2005, “International Differences in the Cost of Equity Capital: Do Legal Institutions and Securities Regulation Matter?”, (ECGI - Law Working Paper No. 15/2003) <http://ssrn.com/abstract=641981>.

may also result in more dispersed equity ownership, greater stock price accuracy and greater liquidity.⁵⁴

More could be done to improve enforcement outcomes. Such improvements may involve legislative change to increase investigation powers and incentives for persons to report market abuse. Another change which may not need legislative intervention would be to restructure the enforcement arms of the ASX and ASIC to work more closely with each other in an effort to ensure that those market abuses that are detected by the ASX become the subject of ASIC enforcement action.

III Improving Investigation Powers and Detection Techniques

The detection and investigation of market misconduct, as with other commercial crime, is intrinsically complex. ASIC already has additional powers not available to other law enforcement bodies, such as State and Federal Police, because of this complexity. Yet paradoxically ASIC does not have access to other powers already available to such law enforcement agencies.

No power to obtain telephone intercepts warrants

Like other enforcement bodies, ASIC can apply for a search warrant for physical evidence under s 3E of the *Crimes Act 1914* (Cth) if it can satisfy a magistrate that there grounds for suspecting that there is, or there will be within the next 72 hours, any material at the premises which will be evidence of any offence.⁵⁵

However currently there is no power for ASIC to obtain a warrant to intercept telephone or other electronic communications in relation to an investigation into market misconduct. Interception without a warrant is prohibited by s.7 of the *Telecommunications (Interception and Access) Act 1979* (Cth) (TI Act). The power to apply for such a warrant is contained in s 39 of the TI Act. Under this section an “enforcement agency”, as defined, can apply to a Judge of the Federal Court or a member of the Administrative Appeals Tribunal (AAT) for a warrant in respect of a particular telecommunication service or in respect of services which may be used by a particular person. ASIC is not however an “enforcement agency” within the definition contained in s 5 of the TI Act. Nor is it possible for any of the enforcement agencies listed within that definition, such as the Australian Federal Police, to obtain a warrant in respect of any of the relevant market misconduct offences in the Corporations Act. This is because s 46 of the TI Act provides that the Judge or AAT member may issue a telecommunications interception warrant on the application of an agency only when they are satisfied that information would be likely to be obtained to assist in connection with the investigation

⁵⁴ L N Beny “Insider Trading Laws and Stock Markets Around the World; An Empirical Contribution to the Theoretical Law and Economics Debate” (2007) 32(2) *Journal of Corporation Law* at 237.

⁵⁵ ASIC can also seek a search warrant under s 35 and s 36 in relation to a failure to produce books in response to a notice. In addition if a company is being wound up ASIC or a liquidator can seek a search warrant under s 530C of the Corporations Act if there is a suspicion that property or books have been concealed or removed. As to ASIC’s powers generally see T Middleton “ASIC’s investigation and enforcement powers – current issues and suggested reforms” (2004) 22 *C&SLJ* 503.

of a “serious offence”. None of the market misconduct offences fall within the definition of “serious offence” in s 5D of the IT Act.

The government has recently introduced legislation into Parliament which would allow the Australian Competition and Consumer Commission (ACCC) to obtain such interception warrants in relation to the investigation of the new provisions to be introduced in the *Trade Practices Act 1974* (Cth) which make it a criminal offence to form a cartel. The stated reason why this power is needed is that:

Cartels are generally covert arrangements. Discover and proof of the existence of a cartel is more difficult than other forms of corporate misconduct, justifying such powers to penetrate the cloak of secrecy.⁵⁶

Insider trading and market manipulation are also usually undertaken under a cloak of secrecy with the use of the telephone and perhaps also the internet to pass information. There may be no documentary trail. That such powers do not exist is an extraordinary impediment to the successful prosecution of misconduct that almost invariably involves the use of the telephone or internet communication. In addition, like cartels, market abuse is often a form of theft, whereby the participant is making a gain at the expense of others in the market. Accordingly there appears to be no reason as to why the market abuse provisions should be treated differently to the cartel offences.

If ASIC was able to obtain a warrant to intercept electronic communication based on a suspicious trading this may result in very significant evidence, perhaps sometimes even direct evidence of the passing of the inside information. In the absence of such evidence ASIC is often left in the exceptionally difficult position of having to try and make out a circumstantial case where it may be able prove that a telephone call was made, but has no evidence as to what was said. In such a scenario it may be difficult for ASIC to prove the trading did not occur for a legitimate reason.

Immunity for participants who ‘blow the whistle’?

The ACCC currently has a policy whereby an individual or a corporation who is involved in a cartel can be granted immunity from civil proceedings provided they are the first person to report the activity to the ACCC, they are not the leader of the cartel and they did not coerce others to join the cartel.⁵⁷ On 1 December 2008 the ACCC and the Commonwealth Director of Public Prosecutions announced a Memorandum of Understanding which has the effect that the same criteria will apply to criminal prosecutions when the new cartel offence provisions are enacted.⁵⁸

⁵⁶ Media Release 27 October 2008 by Hon Chris Bowen Mp Assistant Treasurer “Rudd Government to Introduce Legislation Criminalising Cartels”

<http://assistant.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2008/087.htm&pageID=003&min=ce&Year=&DocType=> viewed 12 December 2008.

⁵⁷ See *ACCC Immunity Policy for Cartel Conduct*, 26 August 2005

<http://www.accc.gov.au/content/index.phtml/itemId/708758> viewed 12 December 2008.

⁵⁸ “ACCC and CDPP Outline Arrangements for Cartel Conduct Immunity” 1 December 2008,

<http://www.cdpp.gov.au/Media/Releases/20081201-ACCC-and-CDPP-Outline-Arrangements-for-Cartel->

David Laurence from the ASX has suggested that ASIC introduce a similar regime for insider trading.⁵⁹ In a recent article “An immunity policy of Insider Trading and Market Manipulation”⁶⁰ Brent Fisse considered whether an immunity policy similar to the ACCC should be introduced by ASIC for market offences. He argues it is difficult to justify why, if such a policy is available for cartel offences it should not be available market offences:

It is difficult to distinguish insider trading from cartel conduct on the basis that the conduct is easier to detect. Market manipulation may be easier to detect given the record of trades from which patterns of manipulation may be discerned but difficulty nonetheless arises.

Nor does it seem plausible to attempt a distinction on the basis of the actual or likely harm to market integrity is less significant in impact than the actual or likely harm to competitive markets from cartel conduct.⁶¹

Fisse also points to the fact that the US Securities Exchange Commission has a leniency policy and the UK Financial Services Authority has a policy of considering cooperation in deciding whether or not to prosecute an individual for market misconduct.⁶²

Whilst such a leniency policy may result in the detection of more market misconduct, by itself, it may prove to be an imperfect mechanism to foster successful enforcement action by ASIC. Without adequate corroboration, it is doubtful that evidence given by the person granted immunity (who would in other circumstances be a co-accused) as to the involvement of another will be sufficient for ASIC to be able to establish a prima facie case. Furthermore, in criminal trials the value of such evidence is lessened by the fact that a jury is likely to be given a warning that such evidence may be unreliable, be told the reasons why it may be unreliable and that the jury must exercise caution in using it to convict an accused.⁶³ Even if ASIC brings civil penalty proceedings, instead of a criminal prosecution, courts have repeatedly stressed that given the seriousness of the consequences for a defendant in such proceedings, a high level of satisfaction is required

[Conduct-Immunity.pdf](#) and draft “Memorandum of Understanding between the Commonwealth Director of Public Prosecutions and the Australian Competition and Consumer Commission regarding Serious Cartel Conduct”, <http://www.cdpp.gov.au/Media/Releases/20081201-ACCC-and-CDPP-Cartel-Conduct-Immunity-MOU.pdf> viewed 12 December 2008.

⁵⁹ E Mayne and D Lawrence “ASX Markets Supervision”, 11th Annual SDIA Conference, Melbourne, 22 May 2008, http://www.asx.com.au/supervision/pdf/sdia_speech_melb_may08_mayne_lawrence.pdf viewed 12 December 2008.

⁶⁰ LCA Corporations Workshop 20-21 September 2008
http://www.brentfisse.com/images/AN_IMMUNITY_POLICY_FOR_INSIDER_TRADING_AND_MARKET_MANIPULATION_LCA_210908.pdf viewed 12 December 2008.

⁶¹ B Fisse “An Immunity Policy for Insider Trading and Market Manipulation?” LCA Corporations Workshop 20-21 September 2008 at 6.
http://www.brentfisse.com/images/AN_IMMUNITY_POLICY_FOR_INSIDER_TRADING_AND_MARKET_MANIPULATION_LCA_210908.pdf viewed 12 December 2008.

⁶² Ibid at 2.

⁶³ See for example Evidence Act 1995 (NSW) s 165.

to find such a contravention.⁶⁴ Evidence of a co-offender without adequate corroboration is unlikely to satisfy this test.

Nevertheless, even though an immunity policy is not likely to be the whole answer, it should be considered given the likely movement towards a more universal system of securities regulation. In such an environment ASIC must be equipped with equivalent powers and tools to those used by equivalent regulators around the world to ensure a more consistent and coordinated enforcement response. In addition if there is an immunity policy and ASIC is given telephone intercept powers, ASIC may be able to use telephone intercepts to obtain the corroboration necessary to secure a conviction. This combination of investigation techniques has the potential to become a powerful tool for ASIC to fight market misconduct.

Bounties for informers?

Another method that is repeatedly raised by academics and other commentators as a possible way by which the number of market misconduct matters ASIC detects and prosecutes each year could be increased is to enable ASIC to pay part of any civil penalties it obtains to a person who provides the information which leads to the successful action.⁶⁵ The SEC currently offers a “bounty for persons who provide information that leads to the recovery of a civil penalty from those who violate the insider trading laws.”⁶⁶

The bounty system was considered in 1989 by the House of Representatives Standing Committee on Legal and Constitutional Affairs, Parliament of Australia (‘Griffiths Committee’) and was rejected due to the fact that evidence from such an informer would be given low weight before courts and juries and accordingly such a system was incompatible with current attitudes in Australia in relation to the credibility of such evidence.⁶⁷ In 2001 the Companies and Securities Advisory Committee (CAMAC) also rejected a system of bounties but on different reasons stating that it was premature to

⁶⁴ See for example *Adler v ASIC* (2003) 46 ACSR 505 at 534; *ASIC v Loiterton* [2004] NSWSC 172 at [10]; *ASIC v Vines* [2002] NSWSC 1222 at [20].

⁶⁵ See for example, comments by J Webster at “Insider trading on the rise-perception or reality?” ASIC Summer School 2008, Sydney, Panel Discussion at 87 at [http://www.fido.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Australias_capital_markets.pdf/\\$file/Australia_capital_markets.pdf](http://www.fido.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Australias_capital_markets.pdf/$file/Australia_capital_markets.pdf), B Fisse “An Immunity Policy for Insider Trading and Market Manipulation?” LCA Corporations Workshop 20-21 September 2008 at 6 http://www.brentfisse.com/images/AN_IMMUNITY_POLICY_FOR_INSIDER_TRADING_AND_MARKET_MANIPULATION_LCA_210908.pdf viewed 12 December 2008 and G Lyon and J J du Plessis *The Law of Insider Trading in Australia*, 2005, The Federation Press, Sydney at 165.

⁶⁶ See SEC Website at <http://www.sec.gov/divisions/enforce/insider.htm>. This is authorised under s 21A(e) of the Securities Exchange Act of 1934.

⁶⁷ House of Representatives Standing Committee on Legal and Constitutional Affairs, Parliament of Australia (Griffiths Committee’) *Fair Shares for All; Insider Trading in Australia* (1989) at 45.

introduce such a system given the then recent introduction of civil penalties for market misconduct.⁶⁸

The introduction of such a system should be considered as part of a review to ensure that ASIC's enforcement powers and methods are consistent with overseas regulators in a world in which we are likely to see an increasing convergence of securities laws. However it is unlikely to prove to be the 'silver bullet' and dramatically increase the number of enforcement actions by ASIC. Such a policy has not substantially contributed to the detection of matters by the SEC. In 1997 the SEC commented that:

The Commissions bounty system has not really developed as a significant source of leads or cases.⁶⁹

More recent figures from the US show that from 1989 until 2006 only four bounty payments were made by the SEC. The reasons seem to be varied and include a reluctance from the SEC to compensate persons for help in its investigations and that the decision to grant a bounty is within the sole discretion of the SEC which is not easy to challenge. In addition payouts are limited to 10% of the amount actually recovered, not the penalty imposed by court, so the payout depends upon the defendant having the capacity to pay. If a criminal prosecution is commenced, instead of civil penalty proceedings, the informer is not eligible for a bounty.⁷⁰

It is likely that there would be similar limitations if ASIC had such a power. ASIC is also likely to be resistant to encouraging a culture whereby persons who report crimes expect some type of reward. There is also likely to be similar problems with defendants' capacity to pay penalties, particularly if a court also makes an order that the defendant compensate any victims.⁷¹ Evidence from witnesses who are to receive a bounty substantially reduces their credibility in court leading to a greater risk that any action based on such evidence will not ultimately be successful. As no penalties are payable on a criminal conviction it will not be available for criminal prosecutions. In addition in 2005 ASIC was severely criticized for bringing civil penalty proceedings instead of a criminal prosecution in a case of insider trading against the high profile defendant, Steve Vizard.⁷² Accordingly ASIC is likely to be reluctant to bring civil penalty proceedings for market misconduct if there is sufficient evidence to support a criminal prosecution.

⁶⁸ CAMAC Insider Trading Discussion Paper (2001) at 87

[http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFDiscussion+Papers/\\$file/Insider_Trading_DP_June_2001.pdf](http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFDiscussion+Papers/$file/Insider_Trading_DP_June_2001.pdf).

⁶⁹ "Special Report – Microcap Fraud, Staffing Issues Top Enforcement Agenda" 29 Securities Regulation and Law Reporter (BNA) 19 December 1997) 1769 at 1722 as quoted in CAMAC Insider Trading Discussion Paper (2001) at 143,

[http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFDiscussion+Papers/\\$file/Insider_Trading_DP_June_2001.pdf](http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFDiscussion+Papers/$file/Insider_Trading_DP_June_2001.pdf)>.

⁷⁰ W P Barrett "Mutiny Over The Bounty" Forbes.com 4 February 2006

http://www.forbes.com/2006/04/19/insider-trading-fraud-cz_wb_0419bounty_print.html viewed 2 December 2008.

⁷¹ See *Corporations Act* 2001 (Cth) s 1317H.

⁷² *ASIC v Vizard* [2005] FCA 1037. For criticism of ASIC's action see for example T McCrann "Insider trading reveals double standards" *The Herald Sun*, 10 July 2005 at 94; S Wilson "Gun-shy ASIC needs to

IV The division of Market Supervision between ASX and ASIC

As is referred to above after ASX detects suspicious trading it then conducts its own investigation before referring the matter to ASIC. The average time taken by the ASX to complete an investigation is 105 days.⁷³ ASIC then assesses whether it should commence an investigation and, if so, refers it to its ‘Enforcement’ team to gather the necessary evidence for legal proceedings to be commenced.⁷⁴

Clearly the merits of this process are that the ASX does some preliminary work on the matter before ASIC becomes involved. ASIC can then analyze this information and focus its investigation resources on the matters which are most likely to lead to a successful enforcement outcome. Another advantage of ASX’s involvement is that it has the technical expertise and market knowledge. In a recent survey commissioned by ASIC only 45% of the businesses surveyed thought that ASIC understands the markets and the people it regulates.⁷⁵ The recent inaction of ASIC to take action on the stock lending practices by Tricom has been pointed to by critics to show that ASIC lacks the ability to recognize problems in the market as they emerge.⁷⁶ In addition with the ASX rather than ASIC funding the surveillance and preliminary investigation, this represents a saving of government resources.

However there is a significant downside to this process in that it invariably results in the duplication of resources and handling of matters. The process described also causes delay between the time of the original misconduct and the point at which ASIC’s investigation swings into action. The longer the delay the greater the risk that evidence will be lost. Emails can be deleted and those on the deleted files on computers, which can often be recovered by forensic computer experts, can be overwritten. Perpetrators may become aware they are under investigation as a result of ASX issuing notices on their brokers. The longer the delay the longer they have to dispose of potential evidentiary material and concoct exculpatory reasons for their actions. Proceeds of crime can be moved to jurisdictions beyond the capacity of Australian courts to capture.

win one” *The Australian*, 19 July 2005 at 22; A Kohler “Make example of the directors they do catch” *The Sydney Morning Herald*, 6 August 2005 at 43; J McCullough “One law for rich, another for Richer” *The Courier –Mail*, 30 July 2005 at 27 and V Comino “The enforcement record of ASIC since the introduction of the civil penalty regime”(2007) 20 AJCL 183.

⁷³ ASX 2008 Annual Report at 30 http://www.asx.com.au/about/pdf/annual_report_2008.pdf, viewed 12 December 2008.

⁷⁴ B Gibson, “Improving confidence and integrity in Australia’s capital markets”, Presentation to the Committee for Economic Development of Australia, 8 July 2008, Sydney [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Integrity_capital_markets_Gibson_July_2008.pdf/\\$file/Integrity_capital_markets_Gibson_July_2008.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Integrity_capital_markets_Gibson_July_2008.pdf/$file/Integrity_capital_markets_Gibson_July_2008.pdf) viewed 12 December 2008

⁷⁵ See The Allen Consulting Group *ASIC Stakeholder Survey*, April 2008 at 16 [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Stakeholder_survey_2008.pdf/\\$file/Stakeholder_survey_2008.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Stakeholder_survey_2008.pdf/$file/Stakeholder_survey_2008.pdf), viewed 16 December 2008.

⁷⁶See for example S Washington “ASIC knew it all but did nothing” *Sydney Morning Herald*”, 28 June 2008 at 41

The studies suggest that insider trading is concentrated around the days and weeks leading up to takeovers, profit announcements and profit warnings. It is at this time offenders are likely to be creating incriminating evidence such as sending emails and making telephone calls. Yet ASIC is unlikely to be investigating the behaviour and using its investigation powers until several months later – substantially increasing the risk of loss of evidential material.

ASIC, perhaps aware of this problem, has publicly stated that it is working with the ASX to speed up the notification of referrals and to minimize the time gap between the alleged conduct and action.⁷⁷ However would it not be more effective for ASIC and ASX to work together from the initial time of the detection of the market misconduct?

Perhaps a solution to this investigation overlap is to make the surveillance and investigation of market offences a joint function of the ASX and ASIC, either through ASIC having a direct interest in ASXSM or for via a new body set up for this purpose. This might alleviate the problems caused by delay and allow ASIC to utilize its powers at an early stage to gather admissible evidence to support enforcement action. With ASX continuing to have a role the ASX's knowledge of the market could still be utilized. The other advantage of a joint body would be that it present less opportunity for 'blame shifting' with both the ASX and ASIC answerable to their shareholders and the public respectively for any failure to effectively regulate the market.

It may be also be opportune to make such a change soon as the ASX is likely to face competition in the future. In the last year ASIC received three applications for licences to compete for trading in ASX listed securities.⁷⁸ As such the Federal Government is considering who will regulate a market where there is more than one licensee, one option being canvassed is to hand all of the surveillance of the market from the ASX to ASIC.⁷⁹ Those in favour of such a hand over believe that as a profit making body ASX does not have the incentive to regulate as it generates income from turnover and, in addition, money spent on regulation results in less profit for ASX shareholders.⁸⁰ Such critics also point to overseas regulators some of whom conduct their own surveillance. For example the Hong Kong Securities & Futures Commission directly monitors the market for market

⁷⁷ T D'Aloisio, "Securities markets, participants and the ASIC" Securities & Derivatives Industry Association Conference, Melbourne, 22 May 2008 at 6 [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Securities%20markets,%20participants%20and%20ASIC.pdf/\\$file/Securities%20markets,%20participants%20and%20ASIC.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Securities%20markets,%20participants%20and%20ASIC.pdf/$file/Securities%20markets,%20participants%20and%20ASIC.pdf) viewed 12 December 2008.

⁷⁸ Ibid at 7.

⁷⁹ See A Moore transcript of interview with the Hon N Sherry, Minister for Superannuation and Corporate Law on ABC Lateline Business, 3 June 2008 <http://minschl.treasurer.gov.au/DisplayDocs.aspx?doc+transcripts/2008/010.htm&pageID+0> viewed 11 December 2008. See also Parliamentary Joint Committee on Corporations and Financial Services "Statutory Oversight of the Australian Securities and Investments Commission" August 2008 at 7 http://www.aph.gov.au/Senate/Committee/corporations_ctte/asic/asic_june_08/report.pdf.

⁸⁰ For a summary of these arguments see J Rydger and C Comerton-Forde "The Importance of Market Integrity, An Analysis of ASX Regulation" 1 September 2004 SIRCA Research at 12-14, http://www.asx.com.au/about/pdf/The_Importance_of_Market_Integrity_-_September_2004.pdf viewed 12 December 2008.

abuse.⁸¹ In response to such criticism supporters of continued surveillance by the ASX assert that the ASX has a strong incentive to maintain high levels of market integrity as such a market is likely to maintain investor confidence and thereby attract a higher level of investment and turnover maximizing profits.⁸²

The restructure of ASXSM or the establishment of a new body utilizing the expertise of the ASX in combination with the investigation powers of ASIC would help to ensure that the aim of maintaining market integrity remains a paramount concern. Such a restructure could also accommodate organisations granted licences to compete with the ASX. These competitors could join the supervisory body, or, alternatively outsource their surveillance and investigation functions to it for a fee. Recently in the US ten exchanges consolidated their insider trading surveillance and investigation efforts to the regulatory arm of the New York Stock Exchange and the Financial Industry Regulatory Authority, a private regulator.⁸³

International enforcement

Such a body may also be able to respond more effectively to the future challenges facing enforcement of securities laws. Regulators are starting to ascertain a trend where securities violations straddle jurisdictional boundaries.⁸⁴ In recognition of this regulators are increasingly entering into and strengthening arrangements with other regulators to share information and assist each other in their enforcement efforts and to work towards a more coordinated response to enforcement. For example in 2008 ASIC and the SEC executed an enhanced Enforcement Memorandum of Understanding allowing greater enforcement cooperation between the SEC and ASIC.⁸⁵ ASIC is also a member of the International Organization of Securities Commissions (IOSCO) and, along with 23 other securities regulators, is a signatory to a Multilateral Memorandum of Understanding to exchange information in relation to market abuse and fraud.⁸⁶

Over time this mutual exchange of information and assistance is likely to become an even more important tool in effectively tackling breaches of securities laws and will represent

⁸¹ See Hong Kong Securities and Futures Commission “Who, What and How We Regulate” <http://www.sfc.hk/sfc/html/EN/aboutsfc/regulate/regulate.html> viewed 12 December 2008.

⁸² For a summary of these arguments see J Rydge and C Comerton-Forde “The Importance of Market Integrity, An Analysis of ASX Regulation” 1 September 2004 SIRCA Research at 12-14, http://www.asx.com.au/about/pdf/The_Importance_of_Market_Integrity_-_September_2004.pdf viewed 12 December 2008.

⁸³ See B Landy “Stock Exchanges Join Forces to Police Insider Trading” Special to the Washington Post, 14 August 2008 at D02.

⁸⁴ See comments of L C Thomsen, Director of Enforcement at the SEC, (2008), “US experience of insider trading enforcement actions” *ASIC Summer School 2008* at 89-96.

⁸⁵ See ASIC Press Release “SEC, Australian authorities sign mutual recognition agreement” 26 August 2008, <http://www.asic.gov.au/asic/asic.nsf/byheadline/08-193+SEC.+Australian+authorities+sign+mutual+recognition+agreement?openDocument>, viewed 16 December 2008

⁸⁶ See International Organization of Securities Commissions *Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information* May 2002 <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD126.pdf>, viewed 16 December 2008.

perhaps one of the most important devices in ASIC's enforcement powers. Yet such arrangements are focused on the exchange of information and assistance from government regulator to government regulator, not private stock exchange to private stock exchange. If ASIC is working with the ASX at the 'coal face' of surveillance and detection of market misconduct as suggested above, in the event that the activity has an overseas aspect, ASIC should be able to quickly use such liaison arrangements with overseas regulators to obtain the information and assistance needed.

Conclusion

Market misconduct appears to be a continuing problem for Australia's markets and tackling such misconduct is crucial to restoring confidence in the markets. As such now may be the time to rethink both ASIC's enforcement powers and the ASX/ASIC division of regulation as part of a strategy to restore such confidence.

Whilst it is realistic to observe that there will probably never be a market free of abuse, what is needed is a continuing process of development and refinement of enforcement responses. In the short term ASIC's powers should be strengthened so that they are at least equivalent to other law enforcement bodies both in Australia and overseas including giving ASIC the ability to apply for telephone interception warrants. In addition the division of market regulation between the ASX and ASIC needs to be changed so that ASIC is involved as soon as a possible contravention is detected. This would allow the use of ASIC's investigation powers at an early stage, increasing the possibility of it obtaining strong admissible evidence which in turn would give ASIC a greater prospect of it being able to bring a successful enforcement action.