STOCK MARKET MANIPULATION TRIALS

AVOIDING THE TRAPS

by

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INTRODUCTION

1. Fiscal offences and their prosecution are very much every day occurrences in today's criminal courts. No longer are those offences confined to theft, obtaining a financial advantage by deception or even social security fraud. More and more frequently the courts are consumed with crimes such as insider trading, misappropriation of trust funds and Ponzi schemes, to name but a few.

2. We now have to deal with the full catalogue of crimes set out in Part 7.10 of the *Corporations Act* with such crimes as false trading and market rigging,[1] false or misleading statements[2] and insider trading.[3] We also have the crime of market manipulation.[4]

3. Our purpose in this paper is to outline some of the more important aspects of the offence of market manipulation from both a theoretical perspective as well as a practical one. We also address the civil recovery of damages from the market manipulator.

ORIGINS OF THE OFFENCE OF MARKET MANIPULATION

4. Unsurprisingly, s 1041A of the *Corporations Act* has its genesis in the futures industry.[5] As long ago as 1986 when the Australian federal legislature was formulating ways to regulate operators in the futures industry,[6] the offence known as "futures market manipulation" was created.[7] The offence of futures market manipulation was taken from experience gained in the United States dating back to the 1920s,[8] with

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[1] Section 1041B.

[2] Section 1041E.

[3] Division 3 of Part 7.10 of Chapter 7.

[4] Section 1041A.

[5] For a discussion of the legislative history of the section see *DPP v JM* [2013] HCA 30 at [44] to [54].

[6] That was achieved by the enactment of the *Futures Industry Act*, 1986.

[7] This was reposed in s 130 of the *Futures Industry Act*, 1986

[8] Commodities trading, in particular, was the subject of regulation.

respect to commodities trading and the regulation of mischief encountered in that forum.

5. Activities in the futures industry were conducted in the Chicago Board of Trade and were controlled by the provisions of the *Commodities Exchange Act*.[9] Unscrupulous traders earned the dubious badge of honour when their skills were described in these terms - "The methods and techniques of manipulation are limited only by the ingenuity of man".[10]

6. At its core the offences created by the *Commodities Exchange Act* and by the *Futures Industry Act* prohibited persons taking part in transactions that had or were likely to have certain consequences to the market.[11] The wording each Act was "had or were likely to have". Proof of the actual suffering of the proscribed conduct was not necessary.

7. The first consequence was *creating* an artificial price for items in the relevant market – futures in the futures market in the case of the *Futures Industry Act* or commodities in the commodities exchange industry in the case of the *Commodities Exchange Act.* So if the impugned conduct had or was likely to have the effect of creating an artificial price for futures or commodities in one of those two markets, then that conduct was criminalized.[12]

8. The second consequence was *maintaining* at a price that was artificial a price for items in the relevant market.[13]

9. Hence, conduct was forbidden if it had (or was likely to have) the effect of *creating* an artificial price or which had (or was likely to have) the effect of *maintaining* an artificial price.[14]

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[9] 7 U.S.C. ss 9 and 13.

[10] [1971] USCA8 443 per Johnsen SCJ, Gibson and Lay CJJ

[11] This was the subject of comment by the High Court in *DPP v JM* [2013] HCA 30 at [50] (per curiam).

[12] *Ibid*

[13] *Ibid*

[14] The emphasis is ours.

10. The offence created under each Act called for a close examination of not only the discrete elements of the conduct but also of the invariably complex commercial setting of the transaction. A person was implicated for "taking part in" a transaction that had one of the two effects already mentioned. The level of participation did not need to be deep. For example, a seller, buyer, agent for either, a broker, an introducer or some other conduit might have been caught so long as the relevant conduct had the necessary causal link of leading to one of the two consequences of "creating" or "maintaining" an "artificial price".

Cargill Inc v Hardin

11. One of the earlier examinations of the elements of market manipulation, then in respect of commodities, was the 1971 decision of the United States Appeals Court in *Cargill Inc v Hardin.*[15] That decision related to trading in wheat futures on the Chicago Board of Trade in 1963. The case is of particular importance as it addressed two concepts that for a time were said to be cornerstones of manipulative conduct, namely the practices of "squeezing" and "cornering".[16] Each practice was noxious as it altered the proper functioning of the market forces of supply and demand.[17]

12. The Eighth Circuit of the Court of Appeals explained[18] that a wheat futures contract to which the *Commodities Exchange Act* applied was one under which a seller agreed to sell and deliver and a purchaser agreed to purchase and receive a quantity of wheat at a specified future date at a specified future price. The buyer who purchased wheat for delivery at a future time had what the industry called a "long position". The seller who sold and was required to deliver the wheat on the specified date was called a "short". Market price for wheat inevitably fluctuated in the period

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[15] [1971] USCA8 443

[16] These activities were mentioned in parliamentary material – see Australia, House of Representatives, *Futures Industry Bill* 1986, Explanatory Memorandum at [258].

[17] This was the subject of comment by the High Court in *DPP v JM* [2013] HCA 30 at [70].

[18] [1971] USCA8 443.

between contract date and delivery and was usually subject to weather variables. Price fluctuations worked certain advantages. For example, if a vendor contracted to sell at a high price and the market price fell between the date of the contract and the date of supply, the seller was able to take the benefit of the high price that he secured even though the market price had fallen in the intervening period. That worked to the seller's advantage. Conversely, buyers in a long position also benefitted where the price of the wheat was above the market price on the delivery date.

13. In May 1963 Cargill Inc wanted to sell a large quantity of wheat to Spanish interests at huge prices. Cargill set about acquiring amounts representing over 60% of the quantity of available wheat. It then offered that wheat for sale. The regulator declared that Cargill had manipulated the market and Cargill appealed that decision.

14. The regulator alleged that Cargill, while holding, had a controlling position and manipulated the market because there was insufficient supply of wheat available for delivery to the market so that when Cargill sold wheat with a view to liquidating its futures contracts it exacted an artificially high price. The regulator contended that Cargill intended to artificially "squeeze" the market.

15. The Court of Appeals determined that Cargill did in fact have a dominant market position. It further held that there was insufficient wheat available from sources other than Cargill for delivery into the market in the latter part of the year. Of greater relevance was the finding that Cargill exacted an artificially high price. As proof of that the court pointed to (a) Cargill attaining record prices in two days of trading in May 1963 when compared to trading movements over the earlier nine years; (b) the spread in two critical years being different when compared to the spread over the preceding nine years and (c) the fact that the price in May 1963 was considerably out of line with futures prices in Kansas over nine prior years. The court held that the price exacted by Cargill for wheat bore no relationship to the cash price of wheat at the relevant time.

16. Taken in combination all those factors led the court to find that Cargill intentionally squeezed and therefore manipulated the market in contravention of the *Commodities Exchange Act*.

17. That was the United States in the 1960s. What of more relevant material closer to home?

North v Marra Developments Ltd

18. The purchase of shares on a stock market for the purpose of setting and maintaining market price came before the High Court of Australia in *North v Marra Developments Ltd,*[19] a case concerning the *Securities Industry Act*. The case is instructive for several reasons, one being that it began as a simple debt claim in which a firm of stock brokers sued for unpaid fees, a claim held to be illegal for contravention of s 70 of the *Securities Industry Act*.

19. To put this in context, the offence with which *North v Marra* was concerned (s 70 of the *Securities Industry Act*) was not identical to s 1041A of the current iteration of the *Corporations Act*. Nor was that section identical to the offence with which *Cargill Inc v Hardin* was concerned (under the *Commodities Exchange Act*). Yet all three had the prohibition against market manipulation in their design.

20. Without going to the precise terms of s 70 of the *Securities Industry Act*, it is enough to say that the offence thereby created was aimed at preventing a false or misleading appearance being created in respect of trading or prices on a stock market.[20] The section was expressed in terms directed to the result of conduct. The section did not proscribe specific acts. Hence the section was expressed in terms that forbad doing anything that created a false or misleading appearance of active trading in securities or doing anything that created a false or misleading appearance with respect to the market or the price of shares.

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[19] (1981) 148 CLR 42

[20] (1981) 148 CLR 42 at [36] (Mason J).

21. North was a firm of stockbrokers and Marra was a property developer. Marra's board become concerned that Marra was vulnerable to takeover so it consulted North for strategic advice on ways to prevent that. North advised Marra to reconstruct its share capital and to take over or merge with another company, Scottish Australia Holdings Ltd. North advised Marra to allot bonus shares so as to bring the value of ordinary shares to $4.40 per share. The trial judge held that North and Marra, by transactions on the Sydney Stock Exchange, established a market for Marra shares at $16.50 for the purpose of their being used in the takeover of Scottish. When the actual price of Marra's shares was $4.40 per share the price of $16.50 was immensely greater. The Court of Appeal later said Marra's purpose was not to buy shares at the lowest price reasonably available and instead Marra bought shares so that the price of Marra's shares would appear publically to be $16.50 and that Marra did so in connection with the takeover of Scottish.[21]

22. The High Court agreed. It held that s 70's purpose was to protect the market from activities that resulted in artificial or managed manipulation.[22] The court held that the section sought to ensure that the market reflected the forces of genuine supply and demand. Buyers or sellers whose transactions were undertaken for the sole or dominant purpose of setting or maintaining the market were not genuine supply and demand forces. The court held that transactions that were real or genuine only in the sense that they were intended to operate according to their terms, like fictitious or colourable transactions, were capable of creating a false or misleading impression as to the market or as to the price.[23] That is because those transactions would not have been entered into were it not for the object on the part of the buyer or seller of setting the price.[24]

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[21] (1981) 148 CLR 42 at [27].
[22] (1981) 148 CLR 42 at [39]
[23] (1981) 148 CLR 42 at [40].
[24] *Ibid.*

23. This much seems redolent of the comments of the Court of Appeals in *Cargill Inc v Hardin* where the court said, "… one of the most common manipulative devices is the floating of false rumours which affect the futures price…"[25]

24. The court held that the false or misleading appearance is that the market, in the absence of any disclosure that market support is afoot, appears to be real or genuine there being no overt sign of market support or manipulation.[26]

25. The court said it was enough to breach the section if the activities were calculated to create a false or misleading appearance and it was not necessary that they did in fact create that appearance.[27]

26. Proof of the commission of the offence does not involve a consideration of profiting by the accused as it is largely irrelevant whether the accused made a profit or not.[28] The concept was explained in *Cargill Inc v Hardin*.[29] It was said that the economic harm done could be just as great whether there had been a profit or a loss.[30] That is important as the fact of there being no profit from the manipulation goes only to sentence and not to proof of the commission of the offence.

27. The forms of market manipulation covered by the *Securities Industry Act* included "false trading", "market rigging", "affecting" and "effecting market prices by fictions" and "false trading and markets". The Act contained a seemingly compendious array of offences. Yet all suffered from an incurable defect. When the methods and techniques of manipulation are limited only by the ingenuity of man, as *Cargill Inc v Hardin* told us, then legislatures seemed always to be behind the eight ball.

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[25] [1971] USCA8 443.
[26] (1981) 148 CLR 42 at [41].
[27] (1981) 148 CLR 42 at [42].
[28] [1971] USCA8 443
[29] *Ibid.*
[30] *Ibid.*

The Corporations Act offences

28. In an attempt to keep pace with the speed of commercial mischief on various markets, in 1989 the Australian federal parliament enacted the provisions called "stock market manipulation" in s 997 of the *Corporations Act* 1989. They were, in reality, a hybrid of the observations drawn from the main themes that emerged from *Cargill Inc v Hardin* and from *North v Marra*. Three main kinds of manipulation were targeted.[31] The first was in s 997(1). It proscribed transactions that had or were likely to have the effect of increasing the price of securities on a stock market with the intent of inducing others to buy or subscribe for the securities of the corporation or a related body.[32]

29. The second was in s 997(4). It forbad transactions that had or were likely to have the effect of reducing the price of securities of a corporation with the intent of inducing others to sell the securities.[33]

30. The third was in s 997(7). It proscribed transactions that had or were likely to have the effect of maintaining or stabilizing the price of securities with the intent of inducing others to sell, buy or subscribe for securities of the corporation.[34]

31. As is evident from the last few passages, intent remained a key to the offences. In *Cargill Inc v Hardin*, the court found that Hardin intentionally caused the squeeze.[35] In *North v Marra* the court focused on s 70, especially on the words "a person shall not create … or do anything which is calculated to create a false or misleading appearance…"[36] The court further held that genuine supply and demand excluded buyers and sellers

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31 These were discussed by the High Court n *DPP v JM* [2013] HCA 30 at [51].

32 *Ibid.*

33 *Ibid.*

34 *Ibid.*

35 [1971] USCA8 443

36 (1981) 148 CLR 42 at [36] et seq.

whose transactions were undertaken for the sole or primary purpose of setting or maintaining the market price.[37]

32. So it was not surprising that the mental elements of the offences with which s 997 was concerned included the purpose of attaining the outcomes mentioned specifically in the three subsections of s 997(1), 997 (4) and 997(7).

33. The *Corporations Act* 2001 re-enacted those three offences in s 997 as well as the offences relating to futures market manipulation, previously set out in the *Futures Industry Act* 1986.[38]

34. That was the regime between 1989 and 2001. With effect from 2002, the *Financial Services Reform Act* 2001 ushered into operation major reforms. It repealed chapters 7 and 8 of the *Corporations Act*, including those potions of the 2001 *Corporations Act* that contained s 997. On 11 March 2002, a new part 7.10 became operative containing the offence of market manipulation, especially s1041A.[39]

SECTION 1041A OF THE CORPORATIONS ACT

35. It must be at once pointed out that insider trading is not the same as market manipulation. The two offences are very different. Section 1041A is concerned with market manipulation only.

36. The section is in these terms –

> **Market manipulation**
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> A person must not take part in, or carry out (whether directly or indirectly and whether in this jurisdiction or elsewhere):
>
> (a) a transaction that has or is likely to have; or
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> (b) 2 or more transactions that have or are likely to have;
>
> the effect of:
>
> (c) creating an artificial price for trading in

[37] (1981) 148 CLR 42 at [39].

[38] This was discussed by the High Court in *DPP v JM* [2013] HCA 30 at [53].

[39] See *DPP v JM* [2013] HCA 30 at [53].

> financial products on a financial market operated in this jurisdiction; or
>
> (d) maintaining at a level that is artificial (whether or not it was previously artificial) a price for trading in financial products on a financial market operated in this jurisdiction.

37. Several things emerge from those deceptively simple few sub-sections. First, the wording is expressed in the conventional mandatory "must not" form. No room exists to argue that the expression is anything but imperative. Next, the degrees of involvement in the impugned activity could not be wider. The section uses descriptive phrases such as "take part in", "carry out", "directly or indirectly" and whether or not in the jurisdiction of the Commonwealth of Australia or elsewhere. That latter point unreservedly foreshadowed the extraterritorial nature of the offence, consonant with the principles espoused in *XYZ v Commonwealth.*[40]

38. Next, the subsections embrace concepts and wording drawn from *Cargill Inc v Hardin* and from *North v Marra* when speaking of "creating" or "maintaining" an artificial price.

39. But the expression "artificial price" was not defined in the legislation and it did not admit of easy interpretation.[41] Nowhere did the legislation say in what respect the price had to be artificial. Nor did the legislation provide for the way in which the artificiality was measured.

40. The Court of Appeal in *CDPP v JM*[42] adopted a construction of s 1041A along similar lines to that in *Cargill* concerning squeezing and cornering. The High Court later rejected that in *CDPP v JM.*[43] The High Court made several observations about the construction of the section that bear close analysis. Below, we set out a few, verbatim.

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[40] (2006) 227 ALR 495.

[41] The consideration the High Court gave to the issue in *DPP v JM* [2013] HCA 30 at [55] to [58] shows this.

[42] [2013] VSCA 21

[43] [2013] HCA 30 at [75].

41. "Because s 1041A prohibits transactions which are likely to have that effect, it is not necessary to demonstrate, whether by some counterfactual analysis or otherwise, that the impugned transactions did create or maintain an artificial price. It is sufficient to show that the buyer or seller set the price with the sole or dominant purpose described".

42. "Participants in the market are entitled to assume that the transactions which are made are made between genuine buyers and sellers and are not made for the purpose of setting or maintaining a particular price."[44]

43. "Contrary to the conclusions of the majority of the Court of Appeal, s 1041A is not confined in its application to the creation or maintenance of an artificial price by a dominant market participant exercising that participant's market power. A purchase of listed share made on the ASX for the sole or at the least dominant purpose of ensuring that the price of the shares was not less than the price paid for that purchase is a transaction which has or is likely to have the effect of creating an artificial price for trading in those share or maintaining at a level that is artificial a price for trading in those shares."[45]

44. What is to be drawn from those statements? The first thing is that anyone – not just a dominant market player - can engage in the impugned conduct. Second, proof that the price of shares was set with the sole or dominant purpose of creating or maintaining an artificial price will suffice. Next, it is not necessary to prove that the transaction did, in fact, create or maintain an artificial price. Finally, it is not necessary to prove that the transaction actually caused genuine buyers or sellers to respond in a certain way.

45. What, then, is an artificial price?

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[44] [2013] HCA 30 at [74].

[45] [2013] HCA 30 at [77].

46. The High Court held in *CDPP v JM*[46] that a price is an "artificial price" if it is a price that results from a transaction in which one party has the sole or dominant purpose of setting or maintaining the price at a particular level and that price does not reflect the forces of genuine supply and demand in an open, informed and efficient market.

PROOFS

47. A careful examination of s 1041A suggests complexity of proofs yet the High Court's decision in *CDPP v JM* suggests that the prosecution's task may not be so difficult. Yet it took the decision of Kaye J in *CDPP v Jacobson*[47] to pronounce upon the matter. Kaye J held that the Crown must prove two things.[48] The first is that the accused intentionally took part in, or carried out, a purchase of share on the ASX. The second is that the sole or dominant purpose of the accused in taking part in or carrying out that purchase was to set or maintain the price of those shares at a particular level.

48. Often, although not always, a contravention of the *Corporations Act* is prosecuted by the Commonwealth Director of Public Prosecutions. Certain consequences flow from that, especially in relation to penalty and sentencing options. However, at this juncture we propose to outline the proofs that the CDPP will ordinarily adduce so as to make out its case in accordance with the ruling of Kaye J in *CDPP v Jacobson*.[49] We also propose to outline some ways the accused can address or meet those proofs.

The role of the accused in the manipulative conduct

49. The first issue is the role and participation of the accused in the transaction. Having regard to the fact that the person placing the trade is

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[46] [2013] HCA 30 at [72].
[47] [2014] VSC 368.
[48] [2014] VSC 368 at [122].
[49] *Ibid.*

as culpable as is his or her client (so long as the requisite intent accompanies the trading) then the broker may be liable as might also be the person on whose instructions the broker trades. A deep understanding of the precise involvement of the accused person is key. Brokers usually undertake a course of study in compliance in the financial services industry so they are not usually involved in market manipulation, although we do know of at least three.

50. More likely will be the situation that the accused is the client of the broker and the accused instructs the broker to trade in a particular manner. Bear in mind that each trade or each transaction usually represents a separate charge, so if the trading activity covers several days or even months, the number of charges might be significant. If the accused is found guilty, the number of charges involved may bear heavily on sentencing. It will also be critical to know how the accused is said to be involved in each transaction, especially in reference to the level of involvement - "directly or indirectly".[50]

51. The accused might also have participated in the transaction or transactions as a conspirator.[51] That will probably involve a consideration of different factual issues when assessing the "taking part in or carrying out" of the transaction.

52. Getting in advance a very detailed explanation of the role of the accused in the relevant transactions is essential.

53. If the accused has been questioned by ASIC in an examination under s 19 of the *Australian Securities and Investment Commission Act* then it is essential to have the transcript of that examination as part of the preparation on behalf of the accused. Time consuming as the task may be, it is critical to obtain instructions from the accused, on a line-by-line basis, to each proposition on which the prosecution relies.

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[50] That is the wording of s 1041A.

[51] In *CDPP v Jacobson* [2014] VSC 368, one of the charges was conspiracy.

Co-operate with the prosecution or fight hard on every point?

54. This is a threshold issue. It will usually fall to be decided according to the strength of the case against the accused. Taking every point is rarely a good strategy and the *Criminal Procedure Act* places a significant onus on counsel and practitioners to ensure that valid points only are run at trial. Time wasting and the pursuit of purposeless points must be jettisoned.

55. This dovetails into the response of the accused to the prosecution's opening.[52] The accused must be candid about the real points that he, she or it will advance at trial. Challenging every point will invariably cause even a patient judge and a tolerant jury to lose control. Not every point calls for challenge whether in the response document or during the trial.

56. That is not to say that the points to be taken should not be advanced with vigour. They should. Precision is needed to ensure that those points are fought hard and are properly articulated in the response of the accused to the summary of the prosecution opening.[53] Care is needed to ensure that uncontroversial points are not challenged in the response document as well as during the running of the case before the jury.

57. Typically, the prosecution will rely on telephone records. Invariably, the fact that those telephone records show the making of calls will not be capable of challenge by the accused. However, the fact that the calls were made is a very different point to the contents of those calls. Challenging the making of the calls is probably unwise but it makes good sense to challenge the contents of the calls, instructions permitting. Emails are a little different as the fact of their sending and the contents of them are not usually capable of challenge. Unless the accused has a forensic basis for challenging emails (both as to the sending and as to the contents thereof) little purpose is served in contesting the emails or in requiring the maker of the email to physically attend court so as to give evidence by telling the jury that he or she wrote the relevant email then sent it.

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[52] This document is required by s 183 of the *Criminal Procedure Act.*

[53] *Ibid.*

58. Of course, there will be occasions when the prosecution's proofs are so poor that by taking every point the accused will enable a later submission to be put that the prosecution has not proved its case beyond reasonable doubt. In those instances the accused must take every point.

Intention

59. Proof of the intention of the accused to artificially set or maintain the price of the shares is the most important component of the case. In a defended prosecution under s 1041A, the accused will invariably challenge the prosecution's assertion that the accused took part in the impugned conduct with the requisite intent. Usually, the accused will not make admissions about intent. The prosecution will mostly rely on inferences to be drawn from other evidence so as to prove the intention of the accused. The form of that other evidence will vary but it is likely to include emails to others (including stockbrokers) with such things as instructions or messages confirming placements of bids or the results of trades. It may also include emails reporting to others about the success or otherwise of trades, a suggestion to increase or decrease bids or asks, or it may include payment transfer details. Letters evidencing those matters will usually be part of the prosecution case.

60. In some cases more direct evidence will be adduced that goes to the heart of intention. That evidence might be led from a person previously convicted for being part of the same transaction, from whom viva voce evidence of alleged conversations is adduced with details of or concerning the transaction. That sort of evidence is excellent for the Crown but it is fraught with the conventional risks when a person previously convicted gives evidence against the accused. Most witnesses of that sort have usually been given an indemnity for the evidence he or she proffers.

61. Evidence from persons who speak about the market and the effect that the conduct of the accused has had on the market requires considerable sensitivity. Rarely will the accused provide instructions that will enable meaningful challenges to be made to that type of evidence. That type of

evidence may well be "expert evidence", properly so called, but the evidence is usually adduced under the guise of evidence from a layperson who has analyzed the market prior to and after the date on which manipulative conduct was said to occur. Simply because it unscrambles commercial and stock broking concepts alien to most members of the jury, this type of evidence is usually well received when adduced by the prosecution and carries with it a correspondingly onerous task for the accused to neutralize the impact that such evidence has on the jury.

Modern sophisticated juries

62. With more and more people becoming involved in small scale share trading, more and more jurors are familiar with the concepts that are raised in market manipulation cases. That said, juries are comprised of people from all walks of life, some of whom have a keen interest in commercial matters whereas others have none. Knowing the degree of detail at which to pitch the case for the accused is never easy.

63. In our experience it is wise to break down the statutory concepts for the jury. Most juries will understand concepts such as "market spreads", "breaking the market" or other share trading jargon so long as the meaning of those concepts is explained to the jury at an early stage of the trial. Conversely, it is unwise to assume that the jury will not follow the evidence or that the jury will be overwhelmed by its detail. Even if the jury misses some of the tiny detail a careful judge will ensure in his or her charge to the jury that those tiny details are brought back to the recall of the jury.

64. For that reason it helps the accused if his or her counsel assists the jury in keeping control of documentary exhibits. Providing a copy of each defence exhibit to each jury member together with a ring binder or lever arch folder into which each exhibit may be placed will help.

Electronic trial

65. More often than not the magnitude of the documents in market manipulation cases is so large that the prosecution converts the documents to electronic images and the trial proceeds electronically with every juror having a computer screen from which to read the documents.

66. That means that counsel for the accused must be sufficiently computer literate to call for and use (using the coded number that corresponds to each document) all and every document to which each witness will be taken, in chief or in cross-examination.

67. In cases of this sort the days of hard copy paper trials is over.

Putting the accused in the witness box

68. By far the most vexing of the issues that confront the legal practitioners in a market manipulation case is whether (circumstances warranting) the accused should give sworn evidence of his or her version of the transaction.

69. Why not, you might think? In our experience it is not so easy.

70. As with most criminal cases, the accused will usually give evidence when he or she is able to give a cogent and rational explanation for the offending which the jury is likely to accept. Of course, the character of the accused and the consequences of putting it in issue are always important matters for the accused.

71. Circumstances permitting, character evidence should be adduced to show that the accused is of good character and therefore less likely to have committed the offence than otherwise.

72. But an accused rolls the dice when entering the witness box. Assuming the accused gives clear and unambiguous evidence in chief, he or she will be amenable to cross-examination where his deeds are laid bare. A

forceful or clever cross-examination can soon erode the credible evidence in chief given by the accused.

73. Naturally, there will be cases where the accused simply cannot stand mute without explaining in his or her words exactly what happened. Those cases put the accused under enormous pressure because the silence of the accused can frequently be more damaging in the eyes of the jury than the risks the accused takes in giving evidence.

Jury issues

74. In the more complex market manipulation cases counsels' final addresses can often be long and the references to the exhibits can be detailed. It is far from uncommon for the trial judge to charge the jury for several days. Equally, in the more complex cases trial judges sometimes invoke the provisions of the *Juries Act* by empanelling more than 12 jurors thereby overcoming the risks and consequences of one or more jurors, during the course of the trial, becoming unable to continue as a juror.

75. As with any criminal trial the time during which the jury deliberates gives no real insight into the likelihood of result. Some verdicts (guilty or not guilty) can be reached quickly whereas others take time. But the usual rule of thumb applies - the longer the deliberation time the more the jury is seriously considering a not guilty verdict.

Sentencing issues

76. Very few cases exist on the sentencing of persons convicted of a breach of s 1041A. In *R v Chan* [2010] VSC 312 T Forrest J sentenced Chan to imprisonment for 20 months for contravening s 1041A but after Chan pleaded guilty.

77. So far as sentencing after a trial is concerned, *CDPP v Jacobson*[54] is the latest authority. After a trial that lasted for 35 sitting days the jury found Jacobson guilty of 35 charges, 33 of which were for individual

[54] [2014] VSC 592

contraventions of s 1041A of the *Corporations Act* and two were for conspiracies associated with those 33 charges. The transactions in which the accused took part were complex, as is revealed by the careful recital of them given by Kaye J in his Honour's sentencing remarks.[55] For the most part the "manipulation" involved the accused instructing his brokers to place bids at or near the close of the market thereby creating the impression that trading in shares in a particular company controlled by the accused was more brisk than it was in fact. The accused engaged in that activity to ensure that the price for certain shares did not drop below a particular price. Any drop below that particular price per share would have triggered margin repayments under various margin-lending facilities into which the accused had previously entered.

78. So far as the sentence was concerned, Kaye J said the offence in s 1041A was serious and that the express object of the section was to promote a fair, orderly and transparent market for registered securities. His Honour said that the section was directed to ensuring that the market price for shares truly reflected the genuine interaction of the forces of supply and demand for those shares in a free market. His Honour said that the offending was not directed to Jacobson obtaining for himself a profit from the resale of the relevant shares at an artificially high price but rather it was to limit his exposure to margin calls.

79. Kaye J said appeal courts had emphasized that the principles of general deterrence and the denunciation of white-collar crimes such as market manipulation must be given significant weight. His Honour said that unless the courts adopt a firm approach in the imposition of sentences for such offences persons minded to commit those offences will consider that the risks in doing so are outweighed by the benefits that accrue from involvement in such offences. His Honour said that considerations of denunciation and general deterrence must be given greater weight than mitigation factors.

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[55] *Ibid.*

80. Kaye J took into account the good character of the accused and the fact that the accused had no history of breaches of the criminal law. The sentence was 20 months imprisonment with the prisoner to be released after 12 month on a recognizance release order of $20,000 (without surety) to be of good behaviour for 12 months.

CIVL REMEDIES AGAINST THE MARKET MANIPULTOR

81. So far we have canvassed the criminal aspects of a prosecution under s 1041A of the *Corporations Act.* The contravener's liability does not stop at the criminal law, however. To better understand how the victim of market manipulation can become a plaintiff suing the market manipulator for compensation requires an investigation of chapter 7 of the *Corporations Act*.

82. The market manipulator's civil liability to compensate the victim for his manipulation has as its genesis s 1317 HA of the *Corporations Act*. In essence, that section provides that in addition to such criminal sanctions the court imposes upon the market manipulator for a contravention of s 1041A, the market manipulator may additionally be liable to compensate any person who suffers damage from the contravention of s 1041A.

83. Section 1317 HA of the *Corporations Act* renames the market manipulator, calling him instead "the liable person". Section 1317 HA then provides that the court may order the liable person to compensate "another person … for damage suffered by that person if the liable person has contravened a financial services civil penalty provision … and the damage has resulted from the contravention."

84. Section 1041A of the *Corporations Act* containing the market manipulation prohibition is part of the financial services civil penalty provisions. Section 1041A is one of the 'civil penalty provisions' enumerated in s 1317E of the *Corporations Act.* There are very many civil

penalty provisions mentioned in that section but for present purposes s 1041A is one of them.

85. In any claim for compensation under s 1317 HA damage must have resulted from the market manipulation. Damage is not defined expect in an inclusionary way to take into account the profit that the market manipulator has made for the acts constituting the contravention.

86. So, if the market manipulator by his contravening conduct procured the result that the relevant shares increased in their price by a certain number of cents per share and the market manipulator thereby derived profit from that increase, then the profit becomes the measuring stick by which the damages are assessed for the purpose of a clam under s 1317 HA.

87. In order for liability to attach to the liable person under s 1317 HA, it is not necessary that the liable person be the subject of a declaration of contravention in relation to a civil penalty under s 1317 E. In other words, a claim for compensation can be commenced with or without there being a claim for declaratory relief under s 1317 E.

88. But something of a conundrum arises where the market manipulator's conduct does not actually have the effect of causing the share price to alter in either direction. Quantification of damages in that situation can be difficult. Aside from issues of causal linkage, the manipulator may very well argue that his conduct was not causative of any loss, *de facto* or *de jure*.

Issuing in a state or a federal court? Commencing a group proceeding?

89. The Supreme Court is seized of jurisdiction to hear and determine cases under s 1317 HA. The Federal Court of Australia is likewise so seized. If the court selected for the proceeding is the Supreme Court, the proceeding is best commenced by writ and statement of claim. The case might take the form of a group proceeding depending on whether seven

or more persons assert that the market manipulator occasioned damage to each. That will be a requisite for a Part 4A group claim.

The detail of the civil proceeding – standard of proof

90. In a claim under s 1317 HA, the plaintiff may need different proofs depending upon whether the alleged market manipulator has already been convicted of a contravention of s 1041A. If the market manipulator has been convicted of an offence against s 1041A, then a certificate of that conviction should suffice as proof of the commission of the acts that are said to represent the contravention of s 1041A.

91. Further, any conviction under s 1041A presupposes that the Crown has proved its case beyond reasonable doubt. The plaintiff will have therefore satisfied the requisite evidentiary standard in any later civil proceeding arising out of the same facts whereby proof to the lower civil standard is required.

92. If the alleged market manipulator has not been convicted of an offence against s 1041A, the plaintiff may nevertheless commence a civil proceeding for damages under s 1317 HA. But any civil proceeding will be stayed pending the hearing and determination of any prosecution for the offence under s 1041A if the prosecution and the civil proceeding arise out of the same facts.

Pleading issues – if the manipulator has been previously convicted

93. Even with a certificate of conviction, in any claim under s 1317 HA the plaintiff will be required to properly plead the elements of his, her or its case for damages that arise from a contravention of s 1041A. If the accused has been previously convicted of a contravention of s 1041A, the focus of a claim under s 1317 HA will be on the damages suffered by the plaintiff rather than the focus being on the elements required to demonstrate the contravention of s 1041A.

94. Ordinarily that will involve the plaintiff alleging –

- the company involved;
- the shares involved, especially if a particular class of shares was involved;
- the relevant period over which the conduct took place;
- the acts said to constitute the market manipulation;
- how the market was affected by the manipulation;
- the way in which the plaintiff has suffered damage;
- any relevant causation issues.

95. The plaintiff will need to plead and prove that the plaintiff has suffered some damage, properly so-called, or that the plaintiff will ultimately suffer some damage. Consonant with general principles of damages, it is conceivable that the phrase "damages" as used in s 1317 HA will include a prospective liability that is yet to crystallize but in respect of which there is no doubt that the plaintiff will become liable. For example, it is likely the plaintiff will have suffered damage if, by reason of the market manipulator's conduct, an event of default is triggered causing the secured creditor to place the company under external administration and to enforce a guarantee given by the plaintiff. In that circumstance the enforcement of the guarantee is the "damage" suffered by the plaintiff. The amount for which the plaintiff is liable in the enforcement of the guarantee becomes his, her or its "damage".

96. As with most damages claims, causation is problematic.

Pleading issues – where the plaintiff has not been convicted under s 1041A

97. If the defendant has not been convicted of an offence under s 1041A of the *Corporations Act*, then the plaintiff in the civil proceeding under s 1317 HA will need to either agree on facts that establish the proofs of the

commission of the offence against s 1041A or the plaintiff will need to formally prove those facts.

98. The first fact to be formally proved is that the market manipulator intentionally took part in or carried out one of more purchases of shares on the ASX. The second fact to be proved is that the sole or dominant purpose of the manipulator's taking part in or carrying out that purchase was to set or maintain the price of those shares at a particular level. Similar considerations apply to those in the proof of the contraventions of s 1041A for the purposes of the criminal offence.

99. As to the requirement that the market manipulator intentionally took part in or carried out one or more purchases of shares on the ASX, the plaintiff will need to identify each such purchase by reference to the manipulator's shares or class of shares involved, the date of each transaction and the number of shares purchased. If the manipulator used someone to purchase in his or her name on the manipulator's behalf then the connection between the named buyer and the manipulator will need to be identified. Manipulators commonly use family members to act as the buyers of the relevant shares and those family members therefore act on the instructions of the manipulator. The element of intention is likely to be satisfied by the fact that the market manipulator actually entered into the transactions for the purchase of the shares.

100. A plaintiff must take care to plead the element of intent required by s 1041A. The section requires proof that the market manipulator's sole or dominant purpose was to set or maintain a price for the shares. The plaintiff must specifically plead that intent and the material facts from which that intent can be distilled. A failure to do so exposes the statement of claim to an application for strike out.

101. The elements set out in paragraph 94 above should also be addressed. In large measure they will form the nucleus of the material facts on which the plaintiff relies.

Discovery

102. An interesting issue may arise if the civil proceeding is commenced prior to a criminal prosecution arising out of the same facts. The whole of the civil proceeding (including any obligation to plead or make discovery) will be stayed while the criminal proceeding based on the same facts is pending.

103. There is no reported decision yet on a civil damages claim under s 1317 HA. In 2010 Justice Goldberg of the Federal Court of Australia decided a civil penalties case in relation to s 1041A and made penalty orders in *ASIC v Soust* [2010] FCA 68. The relief being different the case is useful for information but a civil penalty proceeding is different to a damages proceeding with which s 1317 HA is concerned

Conclusion

100. Recovery of damages under the *Corporations Act* from a market manipulator is unchartered territory. Until the trial of Jacobson any prosecution of the offence to verdict was also unprecedented. This truly is cutting edge law.

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