Market manipulation

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The Dutch Authority for the Financial Markets

The AFM is committed to promoting fair and transparent financial markets.

As an independent market conduct authority, we contribute to a sustainable financial system and prosperity in the Netherlands.

The European Securities and Markets Authority (ESMA) regularly publishes Q&As with regard to the Market Abuse Regulation (MAR). Although the AFM processes this information in its brochures on a regular basis, it may occur that certain information in this document no longer applies. Therefore, we advise you to consult the ESMA website for the latest information on this subject. In case of any uncertainties with regard to interpretations set out in this brochure, you should also consult the Q&As of ESMA.

Click on the following link for a current overview of the latest Q&As:

https://www.esma.europa.eu/questions-and-answers

In this brochure the Q&As of ESMA have been processed up to and including the version of 6 July 2017.

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Introduction

In this brochure the Dutch Authority for the Financial Markets (AFM) explains in more detail the regulations that apply to the prohibition of market manipulation. These regulations result directly from the EU's Market Abuse Regulation (MAR)[1] and have applied since applied since 3 July 2016.

The prohibition of market manipulation is intended to promote the integrity of the financial markets. This means increasing and safeguarding market integrity and investor confidence by promoting the provision of complete, correct and timely available information concerning the trading on financial markets. Trading in financial instruments and prices needs to be the result of legitimate supply and demand arising from investor decisions based on reliable and timely information.

In this brochure[2], the AFM explains in more detail the regulations applying to the prohibition of market manipulation. The prohibition of market manipulation finds its origin in the Market Abuse Directive, 2003/6/EC, and was part of the Wet op het financieel toezicht (Wft). This obligation derives directly from the EU's MAR, which has applied since 3 July 2016. Consequently, the rules in the Wft for the prevention of market abuse have been cancelled and replaced by the MAR.

MiFID II

Where reference in the provisions of the MAR is made to Organised Trading Facilities (OTFs), SME growth markets, emission allowances or auctioned products based thereon, these provisions apply to them as soon as the national legislation implementing Directive 2014/65/EU (MiFID II) comes into force, Directive 2004/39/EC (MiFID) is repealed, and EU regulation 600/2014 (MiFIR) shall apply. Until then, references to MiFID II and MiFIR shall be read as references to MiFID.

The actual text of the EU's Regulation on market abuse can be accessed through the website of the European Commission (http://ec.europa.eu/finance/securities/abuse/index_en.htm).

[1] Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (MAR) and repealing Directive 2003/6/EC of the European Parliament and of the Council, and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC of the Commission.

[2] This brochure has been prepared with the aim of providing the rules applying to market manipulation and the related provisions in more detail. It also contains references to relevant (legal) documents and other sources of information. The purpose of this brochure is to provide information. No rights may be derived from this brochure. Hence no actions should be based solely on its contents. If the text deviates from the MAR, the wording of the MAR prevails.

1. Prohibition of market manipulation

Any person shall not engage in or attempt to engage in market manipulation. The definition of "market manipulation" is described in Article 12 of the MAR. The prohibition of (attempted) market manipulation is described in Article 15 of the MAR.

1.1 Prohibition

Any person shall not engage in or attempt to engage in market manipulation. Market manipulation shall comprise the following activities:

a. entering into a transaction, placing an order to trade or any other behaviour:
    i. which gives, or is likely to give, false or misleading signals as to the supply of, demand for, or price of, a financial instrument, a related spot commodity contract or
    ii. which secures, or is likely to secure, the price of one or several financial instruments, or a related spot commodity contract at an abnormal or artificial level;
b. entering into a transaction, placing an order to trade or any other activity or behaviour which affects, or is likely to affect, the price of one or several financial instruments, a related spot commodity contract or an auctioned product based on emission allowances, which employs a fictitious device or any other form of deception or contrivance;
c. disseminating information through the media, including the Internet, or by any other means, which gives, or is likely to give, false or misleading signals as to the supply of, demand for, or price of, a financial instrument, a related spot commodity contract or an auctioned product based on emission allowances or secures, or is likely to secure, the price of one or several financial instruments, a related spot commodity contract or an auctioned product based on emission allowances at an abnormal or artificial level, including the dissemination of rumours, where the person who made the dissemination knew, or ought to have known, that the information was false or misleading;
d. transmitting false or misleading information or providing false or misleading inputs in relation to a benchmark where the person who made the transmission or provided the input knew or ought to have known that it was false or misleading, or any other behaviour which manipulates the calculation of a benchmark.

1.2 Scope of the prohibition

Pursuant to Articles 2(1) and 2(2) of the MAR, the prohibition of market manipulation applies to the following instruments:

a. financial instruments admitted to trading on a regulated market, or for which admission to trading on a regulated market has been made;
b. financial instruments traded on a Multilateral Trading Facility (MTF), admitted to trading on an MTF or for which admission to trading on an MTF has been made;
c. financial instruments traded on an Organised Trading Facility (OTF);
d. financial instruments not covered by point a, b or c, the price or value of which depends on or has an effect on the price or value of a financial instrument referred to in those points, including, but not limited to, credit default swaps and contracts for difference;
e. emission allowances sold on an auction platform authorised as a regulated market, or other auctioned products based on emission allowances, including auctioned products that are not financial instruments[3];
f. spot commodity contracts, which are not wholesale energy products, where the transaction, order or behaviour has, or is likely or intended to have, an effect on the price or value of a financial instrument referred to in paragraphs a to d;
g. types of financial instruments, including derivative contracts or derivative instruments for the transfer of credit risk, where the transaction, order, bid or behaviour has, or is likely to have, an effect on the price or value of a spot commodity contract where the price or value depends on the price or value of those financial instruments; and
h. behaviour in relation to benchmarks.

The AFM is the competent authority for ensuring compliance with the prohibition of market manipulation in connection with:

- all actions carried out on the territory of the Netherlands; and
- actions carried out abroad relating to instruments admitted to trading on a regulated market, for which a request for admission to trading on such a market has been made, auctioned on an auction platform or which are traded on an MTF or an OTF, or for which a request for admission to trading on an MTF operating within the territory of the Netherlands has been made.

It is irrelevant whether or not the transaction in financial instruments in question is actually carried out through the systems of the market concerned. For example, transactions in bonds that have been admitted to trading on Euronext Amsterdam also come within the scope of the prohibition if such transactions are conducted OTC (over the counter), or via another platform's system.

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[3] Pursuant to Regulation (EU) 1031/2010.

In other words, market manipulation is forbidden whether it takes place in the Netherlands or originates in this country. The prohibition also applies in the case of financial instruments that are not admitted to trading on a regulated market in the Netherlands, but are admitted to trading on a regulated market in another European country.

A transaction is said to take place *in* the Netherlands if it passes through the systems of a market in financial instruments in this country, irrespective of whether the person conducting or arranging the transaction is physically in the Netherlands or some other country. If only the counterparty (to a private transaction) is physically located in the Netherlands, the transaction also qualifies as one conducted in this country.

For a transaction to be deemed as *originating* from the Netherlands, the initiator has to be physically located in the Netherlands when the transaction is carried out or arranged. In this case the transaction passes through the systems of a market in financial instruments outside the Netherlands, or the counterparty is in another country (if the transaction arises from a contract for example). The location of the bank carrying out the transaction is irrelevant, all the more so because the prohibition applies to the person conducting the transaction, and not to the bank.

It is clear from the scope of the prohibition of market manipulation, that it also applies to financial instruments traded on a MTF or an OTF.

2. Exceptions to the prohibition of market manipulation

There are two practices that are exempt from the prohibition of market manipulation, both derived from Articles 5 and 6 of the MAR.

The first exemption applies to 1) trading in own shares under buy-back programmes and to 2) trading in securities or associated instruments for the stabilisation of securities (Article 5 of the MAR).

This provision replaces EU Regulation 2273/2003. Transactions carried out as part of a buy-back programme or the stabilisation of financial securities are exempt, provided they meet the applicable conditions, as well as those concerning transparency. (See Articles 5(1) and 5(4), points a to d, of the MAR).

Besides the conditions, Article 5 of the MAR also specifies the objectives that buy-back programmes must comply with (second paragraph, points a to c). If the objectives and conditions are not met, the exemption cannot be invoked.

The second category of exemptions is for transactions that are part of management activities relating to monetary policy and public debt (Article 6 of the MAR).

3. Justification for false/misleading signals and abnormal/artificial levels

Situations can arise that involve issuing false and/or misleading signals, or creating false and/or artificial levels, where such actions are nevertheless justified.

In the case of:

Entering into a transaction, placing an order to trade or any other behaviour:

i. which gives, or is likely to give, false or misleading signals as to the supply of, demand for, or price of, a financial instrument, a related spot commodity contract; or
ii. which secures, or is likely to secure, the price of one or several financial instruments, or a related spot commodity contract at an abnormal or artificial level;

and providing the person entering into the transaction, placing the order to trade, or engaging in the behaviour can show that his/her reasons for these actions were legitimate reasons and in line with accepted market practices.

Accepted market practices (AMP)

In 2011 an accepted market practice (AMP) regarding the liquidity enhancement contract was established in the Netherlands under the FSA (http://wetten.overheid.nl/BWBR0029964/2011-05-13).

This AMP was terminated on 19 September 2017. Consultation showed there was no interest in continuing the AMP in The Netherlands. Moreover, the Dutch AMP was not or barely not applied by market participants in the past.

4. Indicators of market manipulation

Indicators of manipulative activities are those that send false or misleading signals and keep prices at an abnormal or artificial level.

Leaving aside the types of behaviour summarised in Article 12(3) of the MAR, the application of Article 12(1)(a) leads market participants and competent authorities to consider the indicators given below when they investigate transactions or orders to trade. Note, the list is non-exhaustive, which means that these indicators shall not necessarily be deemed, in themselves, to constitute market manipulation:

a. the extent to which orders to trade given or transactions undertaken represent a significant proportion of the daily volume of transactions in the relevant financial instrument, related spot commodity contract, or auctioned product based on emission allowances, in particular when those activities lead to a significant change in their prices;

b. the extent to which orders to trade given or transactions undertaken by persons with a significant buying or selling position in a financial instrument, related spot commodity contract, or auctioned product based on emission allowances lead to significant changes in the price of that financial instrument, related spot commodity contract, or auctioned product based on emission allowances;

c. whether transactions undertaken lead to no change beneficial ownership of a financial instrument, related spot commodity contract, or auctioned product based on emission allowances;

d. the extent to which orders to trade given or transactions undertaken orders cancelled include position reversals in a short period and represent a significant proportion of the daily volume of transactions in the relevant financial instrument, related spot commodity contract, or auctioned product based on emission allowances, and might be associated with significant changes in the price of a financial instrument, related spot commodity contract, or auctioned product based on emission allowances;

e. the extent to which orders to trade given or transactions undertaken are concentrated within a short time span in the trading session and lead to a price change that is subsequently reversed;

f. the extent to which orders to trade given change the representation of the best bid and offer prices in a financial instrument, related spot commodity contract, or auctioned product based on emission allowances, or more generally in the representation of the order book available to market participants and are removed before they are executed;

g. the extent to which orders to trade given or transactions undertaken at or around a specific time when reference prices, settlement prices and valuations are calculated, and lead to price changes which have an effect on such prices and valuations.

Indicators of manipulative behaviour relating to the employment of fictitious devices or any other form of deception or contrivance.

Leaving aside the types of behaviour summarised in Article 12(2)(3) of the MAR, the application of Article 12(1)(b) leads market participants and competent authorities to consider the indicators given below when they investigate transactions or orders to trade. Note, the list is non-exhaustive which means that these indicators shall not necessarily be deemed, in themselves, to constitute market manipulation:

a. the issue of whether orders to trade given, or transactions undertaken by persons are preceded or followed by the dissemination of false or misleading information by the same persons or by persons linked to them.
b. whether orders to trade are given or transactions are undertaken by persons before or after the same persons or persons linked to them produce or disseminate investment recommendations that are erroneous, biased or demonstrably influenced by material interest.

The signals below could lead the AFM to conduct an investigation. They can also be part of forming an opinion if market manipulation is detected:

- The extent to which the market is disturbed in terms of the number and value of orders and/or transactions compared with the usual size of the market;
- The extent to which the resulting volatility and price deviate from the common market values;
- The extent to which the person conducting the trade has, will gain or lose a dominant market position in the financial instrument concerned;
- The extent to which market transparency is adversely affected by the trading;
- The extent to which the trade improves the risk-return profile of the party conducting the trading is improved as a result of the trading and that of other parties is negatively affected during or as a result of the trading.
- The extent to which additional benefits are sought or achieved through the conduct of the trading in addition to any intention to make a profit or avoid a loss.

5. Examples

This section of the brochure presents a list of examples that could possibly constitute market manipulation:

a) Transactions or orders that produce a false or misleading signal:

- Entering into arrangements for the sale or purchase of financial instruments where there is no change in beneficial interests or market risk, or where the transfer of beneficial interest or market risk is only between parties who are acting in concert or collusion (other than repo transactions and securities lending);
- After institutions have been allocated financial instruments in the primary offering, they purchase these instruments in the secondary market in order to push up the price, and, in so doing, to be able to sell the financial instruments obtained in the primary offering and in the secondary market at a higher price;
- The purchase or sale of financial instruments at the close of the market in order to affect the closing price of the financial instrument concerned;
- The entry of an order or orders with a higher or lower price than the previous order with no intention of execution. The purpose of the orders is to give a misleading impression of demand for or supply of the specific financial instrument. The orders are subsequently cancelled before they are executed;
- Pretending there is market activity by conducting transactions shown on a public trading facility, in order to give the impression of activity or price movement in a financial instrument

b) Transactions or orders designed to bring or maintain a price to an (abnormal) artificial level:

- Large-scale buying or selling of a financial instrument on the expiration date of a related derivative, or vice versa;
- Large-scale buying or selling of a financial instrument on the date when an index is reweighted while already holding a short or long position, in order to profit from the reweighting or change in composition of an index;
- Large-scale buying or selling of a financial instrument at the end of a month, quarter or other reporting period, in order to improve the performance of a portfolio or financial instrument;
- Taking actions to achieve an artificial price level at which other market participants are forced to make delivery, accept delivery or request deferral of delivery in order to meet their obligations in relation to a financial instrument. Such actions are taken by a market participant with a position in a financial instrument and thus have a significant influence on the supply of, demand for, or delivery conditions for that financial instrument or a derivative of that financial instrument;

- Trading in financial instruments in a market with a view to improperly influencing the price of the same or a related financial instrument in another market. This involves influencing the price of correlated financial instruments;
- The consistent prevention of a fall in prices in order to satisfy a credit assessment, bank covenants or other hedge-related purposes;
- The quotation of illogical, excessive or inconsistent bid or offer prices through an intermediary, in order to profit from a lack of competition or liquidity;
- To secure a dominant position over the supply of or demand for a financial instrument which has the effect of fixing, directly or indirectly, purchase or sale prices or creating other unfair trading conditions for the same or a related financial instrument;
- The simultaneous buying and selling of financial instruments by the same person (who is thus trading with himself) at a price that is outside the normal trading bandwidth, in particular if this person at the same time has a position in a related financial instrument (for example, derivatives).

c) Transactions or orders designed to deceive or mislead:

- Actions designed to conceal the actual beneficial interest, so that any kind of reporting requirement is evaded or avoided, or so that no actual information is otherwise disclosed regarding the underlying position in the financial instrument;
- The taking of a long or short position and the subsequent dissemination of a false or misleading positive or negative message, with a view to then closing the position;
- Entering into a position for which a reporting requirement exists, in order to cancel the position immediately after it is reported;
- Taking advantage of access to the media by disseminating an opinion regarding a financial instrument or institution while previously having taken positions in this financial instrument, in order to affect the price of the financial instrument by expressing this opinion without disclosing that one has a conflict of interest.

d) Disseminating misleading or false information:

- The dissemination of false or misleading information regarding a financial instrument or company by means of a press release or by placing a message on a website;
- Issuing misleading signals other than through communications or the media, for example by moving or storing commodities in order to give a false impression of the demand for or supply of a commodity;

In April 2016, the European Commission published a Delegate Regulation[4] that provides, amongst other things, a description of market manipulation indicators more specifically (http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32016R0522).

[4] Delegated Regulation (EU) 2016/522.

6. Interpretations of market manipulation

By "interpretation" the AFM understands a brief, written policy statement that presents its views on specific articles for which the AFM supervises compliance, and/or concerning the powers of the AFM. An interpretation is less extensive than a guideline.

The AFM publishes a variety of interpretations to give market parties an understanding of its views on applicable laws and regulations. Through its contacts with different market parties (including law firms), the AFM signals subjects where there is a need for interpretation.

The AFM has published four interpretations in relation to market manipulation:

- Manipulation by using transactions aimed at influencing prices;
- Manipulation through misleading orders and/or transactions;
- Market manipulation through trading on market orders; and
- Manipulation by using wash trades.

A brochure is available on the AFM's website (*www.afm.nl)* containing detailed descriptions of each of the aforementioned interpretations.

7. Enforcement

Market manipulation is a crime. As such, it is universally forbidden. Not only can other investors suffer direct financial losses as a result of market manipulation, ultimately all citizens can be indirectly affected through their insurances or pension funds. In cases of market manipulation, the AFM can impose a duty backed by an astreinte or can impose a penalty. Serious cases will be referred to the Public Prosecution Service. Infringement of the prohibition of market manipulation is an economic offence.

8. Other elements overlapping the Market Abuse Regulation

Failure to satisfy the obligation to publish inside information in accordance with the notification requirements or the obligation to publish when making investment recommendations can also lead to an infringement of the prohibition of market manipulation Concealing relevant facts in, for instance, a quarterly statement by an issuer, or concealing the existence of one's own position when making an investment recommendation, may constitute market manipulation. These examples could qualify as transactions intended to mislead or deceive, or as the dissemination of false or misleading information.

9. Questions

More information on the market manipulation prohibition is available on the website of the European Commission (http://ec.europa.eu/finance/securities/abuse/index_en.htm).

The AFM is the contact point for questions about market manipulation. For questions and consultations you should send an email to marketsupervision@afm.nl, or call the Monitoring team on +31 (0)20 797 3777.

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