Compliance Notice

Friday 20 December 2019 Reference Number: 0011/19

Subject: Chi-X Australia Compliance Committee Sanctions and Fines OpenMarkets Australia Limited

Decision

The Compliance Committee of Chi-X Australia has sanctioned OpenMarkets Australia Limited (OM) and imposed a fine of $20,000 in relation to OM trading on behalf of an offshore-based day trading client (referred to herein as 'the client'), in the period December 2018 to February 2019. The Committee found that the trading contravened Operating Rule 3.1(e) by prejudicing the fair and orderly operation of the Chi-X market.

The Committee is of the view that the sanction and fine will serve as a deterrence to other Participants from engaging in trading on behalf of similar clients, without first ensuring that there is a complete suite of alerts and other controls in place to detect and prevent trading that may prejudice the fair and orderly operation of the Chi-X market.

The Trading

In the period December 2018 to February 2019, OM engaged in trading on behalf of the client that involved the following trading patterns:

(a) The initial opening of a long position through multiple buy orders;

(b) Closing out the long position through multiple sell orders later that same day at prices higher than those at which the position had been opened;

(c) At the same time a relatively large volume sell order was entered on the Chi-X order book by OM on behalf of that client, a relatively lower volume buy order was submitted at a higher price on the ASX order book; and

(d) The buy order referenced in (c) was often only in the market for a short time, being deleted immediately after the lower priced ask had been filled on the Chi-X market.

Chi-X received complaints in relation to the trading.

<u>The Client</u>

The client on whose behalf OM conducted trading had been the subject of a prior disciplinary notice issued by an offshore regulator, in which it was stated:

> *Intraday spoofing involves the use of non-bona fide orders, or orders that the trader does not intend to have executed, to induce others to buy or sell the security at a price not representative of actual supply or demand. More specifically, a trader places a non-bona fide buy (or sell) order. If that order is followed by another market participant, the trader will then enter a number of non-bona fide buy (or sell) orders for the purpose of attracting interest to that side of the order book. These non-bona fide orders are not intended to be executed. The purpose of these non-bona fide orders is to create a false impression of interest on that side of the order book. The trader will then enter an order for execution on the other side of the market at the better price. Either before or immediately after switching sides to trade, the trader cancels the open, non-bona fide orders and the quote returns to the pre-spoofing level.*
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> *More specifically, [the client] engaged in intraday spoofing on certain days in the Material Time by executing the following pattern in quick succession:*
>
> *(a) Posting orders that improved the National Best Bid ("NBB") or National Best Offer ("NBO") in increments at a time, waiting for another market participant to react and then repeating until the NBB or NBO reached a price at which the [the client] trader would like to trade or until the counterparty stopped following;*
>
> *(b) After inducing or baiting other market participants to increase or decrease the price of their bids or offers, the [the client] trader then entered an active order on the other side of the market to trade at the better price;*
>
> *(c) The [trader] then cancelled the baiting orders shortly before or after the trades; and*
>
> *(d) As a result of the cancellation by the [trader], the quote returned to the pre-spoofing level.*
>
> *20. As a result of this trading pattern, trades were executed at artificial prices because the fill of the order described in paragraph 19(b) above took place at a higher price (or lower) than the NBB/NBO before the non bona fide orders were entered by the trader. These orders were intended to deceive and did deceive certain counterparties into buying (or selling) stocks from (or to) the trader at prices that had been artificially raised (or lowered) by the trader.*
>
> *21. This process was usually repeated multiple times on the same day.*

OM confirmed that it was aware of this Notice.

<u>Matters taken into account by the Committee</u>

The Committee took into account the following in deciding upon the appropriate fine and sanction.

- OM took a number of steps in an attempt to have appropriate systems and controls in place in respect of the trading patterns, including:

  (a) detailed discussions with the client in December 2015 and January 2016 regarding the client's trading controls;

  (b) independent testing of the client's systems for the application of layering and spoofing tools;

(c) the COO of OM at the time liaised with the client and Iress in December 2015 and January 2016 for the purpose of implementing system changes; and

(d) an internal and external review of the SMARTs filters and post trade monitoring and surveillance at OM, including in respect of trading by the client.

- On 27 February 2019, OM changed the configuration of order routing available to its client to prevent it from posting orders that would cross the ASX and Chi-X markets.
- The disciplinary record of OM, including the infringement notice issued by the Markets Disciplinary Panel – see here.
- OM cooperated in the investigation and did not contest this outcome.
- The trading had the potential to damage the reputation and integrity of Australia's regulated markets.
- The availability of an alert and process to detect and prevent repeat occurrences of the trading.
- The complaints received by Chi-X in relation to the trading.
- The repeated occurrences of the trading pattern over the relevant period.

Guidelines Applied

The Committee was of the view that the trading involved a serious contravention of the Operating Rules but that OM had taken steps to improve its systems in this area and had also co-operated with the current investigation and disciplinary process.

The Committee is of the view that the sanction will serve as a deterrence to other Participants from engaging in trading on behalf of similar clients without ensuring that there is a complete suite of appropriate alerts and other controls in place to detect and prevent trading that may prejudice the fair and orderly operation of the Chi-X markets.