

**Participant Circular****Date:** 11 August 2003**Key topics**

1. Joseph Palmer & Sons
2. Lonsdale Securities Limited

Reading List

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Compliance Managers
DTR Operators
Managing Directors
Office Managers
Operations Managers (back office)

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DISCIPLINARY MATTERS

The Australian Stock Exchange Limited's National Adjudicatory Tribunal (**"The Tribunal"**) has determined the following:

Joseph Palmer and Sons ("Joseph Palmer") has been fined:

- (i) \$40,000 (plus GST) for a breach of ASX Business Rule 2.2.4(1)(a)(ii) in respect of certain dealings as Principal in Harbour Capital Limited ordinary shares (**"HBR"**) on 31 January, 28 February, 30 March, 31 May and 29 June 2001; and
- (ii) \$5,000 (plus GST) for a breach of old ASX Business Rule 1.2.1(ii), in that during 1 January and 2 July 2001, Joseph Palmer failed to maintain accurate records of certain orders received for the purchase and sale of shares in HBR (this matter was not contested by Joseph Palmer).

The circumstances of this matter are as follows:

The breach of ASX Business Rule 2.2.4(1)(a)(ii) on 31 January, 28 February, 30 March, 31 May and 29 June 2001 involved Joseph Palmer dealing as Principal in HBR on the last trading day in each respective month (**"the End of Month Conduct"**).

Dealing on 31 January 2001

Immediately prior to 10:03:10 on 31 January 2001 the market for HBR was Bid \$0.45/\$0.48 Offer with a last traded price of \$0.48 per share. Joseph Palmer as Principal maintained the priority Bid in SEATS, with a Bid to buy 800 HBR at \$0.45 per share. At 10:03:10 Joseph Palmer cancelled its Bid as Principal to buy 800 HBR at \$0.45 per share and a short time later at 10:03:21 and 10:03:35 respectively, Joseph Palmer entered Offers on behalf of clients to sell 7,320 and 14,641 HBR at \$0.45 per share.

Joseph Palmer's removal of its Bid to buy 800 HBR at \$0.45 per share, at the time it had two client orders to sell HBR at \$0.45 per share, prevented Joseph Palmer as Principal crossing 800 HBR at \$0.45 per share to a client in the SEATS Opening phase. There was no trading in HBR on 31 January 2001. The last traded price for HBR in January 2001 was \$0.48 per share (that resulted from a trade on 30 January 2001).

Dealing on 28 February 2001

At 13:49:43 on 28 February 2001 Joseph Palmer amended an existing Offer it maintained in SEATS on behalf of a client to sell 2,043 HBR at \$0.40 per share, to an Offer to sell 2,043 HBR at \$0.43 per share (at 14:12:59 this became the priority Offer in SEATS). At 15:33:10 on 28 February 2001 Joseph Palmer entered a further Offer in SEATS to sell 915 HBR at \$0.43 per share on behalf of a client.

At 15:59:14 Joseph Palmer entered a Bid in SEATS as Principal to buy 2,958 HBR at \$0.43 per share that immediately traded with Joseph Palmer's Offers to sell 2,043 HBR and 915 HBR at \$0.43 per share. Joseph Palmer by entering its Bid for 2,958 HBR at \$0.43 per share increased the last traded price for HBR on 28 February 2001 from \$0.36 per share to \$0.43 per share. This trading was the last trading in HBR in February 2001.

Dealing on 30 March 2001

At 15:49:35 on 30 March 2001, Joseph Palmer as Principal amended its priority Bid to buy 13,611 HBR at \$0.36 per share to a Bid to buy 12,000 HBR at \$0.36 per share.

At 15:50:16 Joseph Palmer entered a Bid in SEATS as Principal to buy 1,611 HBR at \$0.42 per share which became the priority Bid in the market for HBR which was Bid \$0.42/\$0.45 Offer with a last traded price of \$0.36 per share.

At 16:12:33 during the Pre-open prior to the Closing Single Price Auction, Joseph Palmer as Principal amended its Bid to buy 1,611 HBR at \$0.42 per share to a Bid for 1,611 HBR at \$0.45 per share. At 16:15:01 during the Closing Single Price Auction, Joseph Palmer purchased a total of 1,611 HBR at \$0.45 per share in two trades. Joseph Palmer as Principal by amending its Bid increased the last traded price for HBR on 30 March 2001 from \$0.36 per share to \$0.45 per share. This trading was the last trading in HBR in March 2001.

Dealing on 31 May 2001

At 14:59:11 on 31 May 2001 Joseph Palmer entered an Offer to sell 890 HBR at \$0.42 per share in SEATS on behalf of a client. This became the priority Offer in the market for HBR which was Bid \$0.38/\$0.42 Offer with a last traded price of \$0.375 per share.

At 15:28:47 Joseph Palmer as Principal entered a Bid in SEATS to buy 890 HBR at \$0.42 per share that resulted in Joseph Palmer as Principal buying 890 HBR at \$0.42 per share from its client. This was the last trade in HBR in May 2001. Joseph Palmer by entering its Bid to buy 890 HBR at \$0.42 per share increased the last traded price for HBR on 31 May 2001 from \$0.375 to \$0.42 per share.

Dealing on 29 June 2001.

At 15:48:55 on 29 June 2001, when the market for HBR was Bid \$0.39/\$0.45 Offer with a last traded price of \$0.37 per share, Joseph Palmer as Principal entered a Bid in SEATS to buy 2,031 HBR at \$0.40 per share (this became the priority Bid). At 15:58:20 as a result of another Trading Participant entering an Offer in SEATS to sell 5,000 HBR at \$0.42 per share, the market for HBR became Bid \$0.40/\$0.42 Offer.

At 16:04:02 during the SEATS Pre-open phase prior to the Closing Single Price Auction, Joseph Palmer amended its Bid as Principal to a Bid to buy 2,031 HBR at \$0.42 cents per share.

At 16:05:25 another Trading Participant amended a Bid in SEATS, to a Bid to buy 4,291 HBR at \$0.42 per share. This Bid became the second priority Bid, behind the Bid of Joseph Palmer, in the market for HBR which was Bid \$0.42/\$0.42 Offer.

At 16:12:02 Joseph Palmer amended its priority Bid as Principal to buy 2,031 HBR at \$0.42 per share, to a Bid to buy 2,031 HBR at \$0.40 per share, thereby losing priority. There was no further activity in the market for HBR on 29 June 2001, until the Closing Single Price Auction that occurred at 16:15:01, at which time there was one trade in HBR for 4,291 HBR at \$0.42 per share. This trade increased the last traded price for HBR from \$0.37 per share to \$0.42 per share, but did not involve Joseph Palmer.

The Tribunal determined

- (a) Joseph Palmer dealt in HBR in SEATS as Principal and that dealing had the effect, or likely effect of creating a false or misleading appearance of active trading in HBR or with respect to the market for HBR, or the price of HBR;

- (b) The effect, or likely effect, of the End of Month Conduct was:
- (i) to result in the last trade price for HBR to remain as high as possible, but at least in excess of \$0.40 on the last trading day of each month – the effect was a direct result of the End of Month Conduct;
 - (ii) to maintain, to the extent possible, a price for HBR exceeding \$0.40;
 - (iii) to maintain or strengthen the market for HBR on the last trading day of each month; and/or
 - (iv) to maintain or strengthen the market for, and the price of, HBR generally so as to arrest or slow the decline that was in evidence in the last half of 2000; and/or
 - (v) to alter the composition of the market for HBR as it previously existed; and
- (c) The End of Month Conduct either created, or was likely to create, a false and/or misleading appearance for the following reasons:
- (i) its timing was such so as to deflect the possibility of the price of HBR being sold down;
 - (ii) it involved crossing a significant market spread so as to increase the price of HBR, on a number of occasions;
 - (iii) it involved the cancellation of a Bid that would have been immediately matched and which would have reduced the end of month price of HBR from \$0.48 to \$0.45 per share;
 - (iv) but for the End of Month conduct, the market for HBR would have reflected different supply and demand parameters during the relevant period; and
 - (v) but for the End of the Month Conduct, the prices for HBR during the relevant period would have been lower than they were, at least on the last trading days of January, February, March and May. It is also likely that the prices for HBR would have been lower as they in fact were for much of the relevant period.

The Tribunal also found Joseph Palmer's records relating to orders received to deal in HBR were deficient in the following respects:

- (a) In nine order records the name of the natural person placing the order was not recorded;
- (b) In one order record price related instructions were not recorded;
- (c) In eight order records the date and time was not, or not correctly recorded; and
- (d) In one order record the name of the person receiving the order was not recorded.

In determining the appropriate penalty for these breaches the Tribunal noted that in respect of the End of Month Conduct:

- (a) Joseph Palmer did not admit it had breached the ASX Business Rule;
- (b) Joseph Palmer engaged in the dealings as Principal;
- (c) Joseph Palmer's conduct was of a nature that clearly fell within the types of dealing identified in ASX Business Rule 2.2.4(2) and ASX Guidance Note 8/00 so that it should have been readily apparent to Joseph Palmer that the conduct was likely to offend Rule 2.2.4(1)(a)(ii); and
- (d) the End of Month Conduct was very serious misconduct and was deserving of a substantial penalty.

The Tribunal considered that accurate order record keeping is a fundamental obligation for Trading Participants because accurate records assist in creating an audit trail, promote good business practice and establish client instructions in the event of a dispute.

Lonsdale Securities Limited ("LSL") has been fined a total of \$25,000.00 (plus GST) by the Tribunal in relation to a breach of ASX Business Rule 2.2.2(4)(a) and a breach of ASX Business Rule 2.2.1(7). LSL elected not to contest the charges.

The circumstances of this matter are as follows:

Breach of ASX Business Rule 2.2.2(4)(a)

1. In early 2001 LSL developed a web-based Internet order placement system for licensed dealers (financial planners), enabling them to place orders on behalf of their clients by way of Automated Client Order Processing ("**ACOP**").
2. In this regard LSL operated an Automated Order Processing System ("**AOP**") during the period 26 September 2001 to 13 March 2002 (inclusive). Prior to using its AOP system, LSL failed to provide to the Exchange certification (in the form prescribed by the Exchange from an appropriately qualified independent person), as it was required to do in order to comply with Rule 2.2.2 (1).

Breach of ASX Business Rule 2.2.1(7)

1. During the period 26 September 2001 to 13 March 2002 (inclusive), LSL did not, as required by Rule 2.2.1(7), maintain and enforce at all times appropriate security procedures with respect to its AOP system.
2. On or about 12 September 2001 LSL received a report from its independent expert ("**the Report**") with respect to its compliance with ASX Business Rule 2.2.2(1). The Report contained a number of exceptions ("**Exceptions**") with respect to the AOP System's compliance with ASX Business Rule 2.2.2(1), identifying weaknesses concerning the security procedures for LSL's AOP system and accordingly did not amount to a certification for the purposes of Rule 2.2.2(4)(a);
3. On 26 September 2001, LSL commenced ACOP operations.
4. Included amongst the Exceptions was the possibility that the AOP System was at risk with respect to the entry of unauthorised trades directly into the market. LSL failed to adequately address that risk prior to the commencement of operation of its AOP system.

The Tribunal considered the breaches by LSL of ASX Business Rules 2.2.2(4)(a) and 2.2.1(7) to be serious matters. The Tribunal noted LSL's assurances to the ASX that it was not aware of any security breaches having occurred during operation of their ACOP, and the Tribunal also noted that LSL from the outset did not contest the breaches and fully co-operated with ASX with respect to these matters. Accordingly the Tribunal imposed a lesser fine than otherwise would have been imposed.