



ASX Circular

Date: 9 December 2010

Key topics

- Merrill Lynch Equities (Australia) Limited

Reading List

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

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DISCIPLINARY MATTERS

The ASX Disciplinary Tribunal (the 'Tribunal') has determined the following:

Merrill Lynch Equities (Australia) Limited ('MLEAL') contravened the following ASX Market Rules*:

- ASX Market Rule 13.1.5(a)(i) and thereby ASX Market Rule 13.1.4(a) on 30 September 2008, in failing to have in place the necessary organisational and/or technical resources to ensure that the trading messages submitted in relation to 22 securities (the 'Relevant Securities') did not interfere with the integrity of the equities market operated by ASX. ('Contravention 1');
- ASX Market Rule 4.1.1 by engaging in conduct on 30 September 2008 which involved a substantial and consistent failure to reach reasonable standards of competence and diligence and which was or could reasonably be considered as likely to have been prejudicial to the interests of ASX or its market participants ('Contravention 2').

MLEAL did not contest the contraventions before the Tribunal.

The Tribunal imposed a total fine of \$200,000 (plus GST).

The circumstances of the matter are detailed as follows:

This matter involved trading by MLEAL in relation to the Relevant Securities on 30 September 2008. On that day MLEAL, on behalf of its client (the 'Client'), made a series of bids for one share in each of the 22 Relevant Securities, establishing a higher closing price in each security (the 'Relevant Securities Trading').

As a result of the difference between the bid price and the last price for each Relevant Security, the orders were diverted for consideration by an MLEAL Designated Trading Representative ('DTR'). The bid was authorised by the DTR on each occasion for entry into the market.

Attachment A sets out the details of the Relevant Securities Trading.

Prior to the Relevant Securities Trading, and as a result of previous similar trading by the Client, MLEAL knew or ought to have known of the potential for the Client's trading to interfere with the efficiency and/or integrity of the ASX equities market.

The submission of the trading messages in respect of the Relevant Securities on 30 September 2008 interfered with the integrity of the equities market operated by ASX because:

- each relevant securities transaction had a significant impact on the price of the relevant security;
- in each case the price impact resulted from the purchase of a single share;
- the conduct continued over a prolonged period during the afternoon of 30 September 2008;
- the conduct involved 22 separate securities;

- parties wishing to invest in or observing the market in the Relevant Securities could not have been confident that the post transaction prices of the Relevant Securities were a genuine reflection of supply, demand and information.

MLEAL failed to have and maintain the necessary organisational and technical resources to ensure that the trading messages it submitted in respect of the Relevant Securities did not interfere with the integrity of the equities market operated by ASX in that, notwithstanding its state of knowledge on 30 September 2008, MLEAL:

- failed to put in place any, or any adequate, arrangements to prevent trading by its Client that might interfere with the integrity of the equities market operated by ASX;
- failed to adequately warn, train, advise or otherwise ensure that, in respect of trading by its Client, its DTR would not submit trading messages that might interfere with the integrity of the equities market operated by ASX;
- failed to query its Client at the time about its orders for the Relevant Securities or prevent the continued transmission of trading messages in respect of orders entered by the Client with similar characteristics. It also failed to query or cancel orders already entered; and
- permitted a DTR to review the Client's orders for the Relevant Securities when he was incompetent to do so given those orders interfered with the integrity of the market operated by ASX.

In addition, MLEAL's conduct:

- demonstrated a disregard for the fundamental importance of the integrity of the market and MLEAL's wider obligations to ASX and other participants;
- in relation to the trading on 30 September 2008 fell below reasonable standards of competence and diligence as required by Rule 4.1.1(w); and
- could reasonably be considered as likely to have been prejudicial to the interests of ASX or its market participants in breach of Market Rule 4.1.1(w).

In determining penalty, the Tribunal, took into account a number of matters, including the following:

- the circumstances and seriousness of the contraventions;
- the disciplinary history of MLEAL having had numerous unrelated disciplinary sanctions recorded against it by the Tribunal, including matters which have involved serious contraventions carrying substantial penalties. MLEAL has been sanctioned by the Tribunal on ten occasions since 2002;
- the contravening conduct was indicative of a pattern of non-compliance;
- the misconduct had the potential to damage the reputation and integrity of the ASX and the market and facilities it operates;
- MLEAL fully co-operated with ASX in relation to the conduct of its investigation into the matter;
- MLEAL agreed at an early stage not to contest the Contraventions, thereby saving time and costs; and
- that while at the time of the contravention MLEAL did not have appropriate controls in place to ensure compliance with the relevant rules, MLEAL has taken significant remedial action to prevent a recurrence of the contravention through the upgrading of the corporate governance, risk management, supervision and compliance structures of MLEAL (the 'Project'). The Project included:
 - hiring (including at senior levels) across business, risk and compliance functions;
 - revised and updated policies and procedures;
 - a thorough risk assessment of all the MLEAL businesses, concentrating on general risks, rule-based risks and regulatory obligations;
 - an enhanced corporate governance model;
 - extensive training programs touching on key obligations of DTRs, Responsible Executives and staff generally;
 - enhanced business supervision, monitoring and surveillance programs; and
 - a post implementation review of the Project that was conducted by an accounting firm. The review did not identify any significant negative findings.

Disciplinary Tribunal Sanction Guidelines

As the contravening conduct occurred after 31 March 2008 (but prior to 1 August 2010)*, that being the effective time under the ASX Disciplinary Processes and Appeals Rulebook (the 'Rulebook'), the Tribunal was bound by the sanction guidelines (Annexure A to the Rulebook Procedures) in making its determination as to sanction in this matter.

In accordance with the sanction guidelines at Annexure A, the Tribunal determined that Contraventions 1 and 2 were appropriately classified as a Level 2 (Serious Contravention) and a Level 3 (Very Serious Contravention), for which the applicable penalty ranges are \$20,000 - \$100,000 (plus GST) and \$100,000 - \$1,000,000, respectively.

The Tribunal considered the aggravating and the mitigating circumstances in each contravention, and considers that a total fine of \$200,000 (plus GST) represents an appropriate sanction in the circumstances. The Tribunal intends to send a clear message to market participants regarding the seriousness of these contraventions. The Tribunal considers that the imposition of this fine appropriately serves the purposes of deterring future misconduct by MLEAL and other participants, protecting the interests of ASX and its participating organisations and of promoting confidence in the integrity of the market. The Tribunal emphasises the importance of MLEAL ensuring that it has appropriate measures in place to prevent any further misconduct.

*On 1 August 2010, the supervision of trading on Australia's domestic licensed markets and the supervision of trading participants transferred from ASX to the Australian Securities and Investments Commission (ASIC). The conduct that is the subject of these contraventions occurred prior to the transfer date. ASX will continue to manage, and bring before the Tribunal, disciplinary matters for potential breaches of its operating rules occurring before the transfer date.

As part of the transfer, a number of changes were made to the rules, including the replacement of the ASX Market Rules by the ASX Operating Rules (administered by ASX) and the ASIC Market Integrity Rules (ASX Market) (administered by ASIC). Potential operating rule breaches which occurred prior to 1 August 2010 will be dealt with in accordance with the rules in place at the time of the alleged breach.

Attachment A

| No. | Approximate time on 30 September 2008 | Order | Bid/Ask/Last | Price impact (%) |
|-----|---------------------------------------|------------------|-------------------------|------------------|
| 1. | 13:15 | 1 AFR at \$0.059 | \$0.043/\$0.055/\$0.045 | 22.22% |
| 2. | 13:46 | 1 AKK at \$0.175 | \$0.14/\$0.155/\$0.14 | 10.71% |
| 3. | 13:54 | 1 ANH at \$0.017 | \$0.012/\$0.013/\$0.012 | 8.33% |
| 4. | 14:00 | 1 ARA at \$0.40 | \$0.35/\$0.38/\$0.35 | 8.57% |
| 5. | 14:09 | 1 BTC at \$0.165 | \$0.13/\$0.145/\$0.13 | 11.54% |
| 6. | 14:29 | 1 BNE at \$0.305 | \$0.22/\$0.285/\$0.26 | 9.62% |
| 7. | 14:37 | 1 GFE at \$0.24 | \$0.11/\$0.22/\$0.11 | 100% |
| 8. | 14:38 | 1 GFL at \$0.97 | \$0.87/\$0.95/\$0.87 | 9.2% |
| 9. | 14:39 | 1 GLB at \$0.48 | \$0.43/\$0.46/\$0.43 | 6.98% |
| 10. | 14:42 | 1 GYN at \$0.14 | \$0.07/\$0.12/\$0.10 | 20% |
| 11. | 14:42 | 1 HGN at \$0.315 | \$0.25/\$0.295/\$0.25 | 18% |
| 12. | 14:43 | 1 HIP at \$1.32 | \$1.27/\$1.30/\$1.215 | 7% |
| 13. | 14:43 | 1 HTW at \$0.64 | \$0.595/\$0.62/\$0.595 | 4.2% |
| 14. | 14:47 | 1 NSN at \$1.22 | \$1.11/\$1.20/\$1.11 | 8.11% |
| 15. | 14:48 | 1 LMC at \$3.84 | \$3.50/\$3.80/\$3.50 | 8.57% |
| 16. | 14:49 | 1 MCH at \$1.52 | \$1.00/\$1.50/\$1.26 | 19.05% |
| 17. | 14:54 | 1 NAM at \$0.32 | \$0.29/\$0.30/\$0.29 | 3.45% |
| 18. | 14:54 | 1 NUP at \$0.16 | \$0.08/\$0.14/\$0.08 | 75% |
| 19. | 14:57 | 1 PLB at \$0.77 | \$0.64/\$0.75/\$0.68 | 10.29% |
| 20. | 15:05 | 1 PRZ at \$0.20 | \$0.17/\$0.18/\$0.17 | 5.88% |
| 21. | 15:06 | 1 RDM at \$0.17 | \$0.13/\$0.15/\$0.14 | 7.14% |
| 22. | 15:07 | 1 RHL at \$4.24 | \$4.10/\$4.20/\$4.00 | 5% |