Common Origins, Different Destinies:

Investors’ Rights against Market Manipulation in the U.K., Australia and Singapore

Abstract
The regulatory rules against manipulation in the U.K., Australia and Singapore have moved steadily toward formulations that ease the burdens of prosecution. Yet, the drive toward stronger regulatory protections against market manipulation does not necessarily translate into more robust private rights of action. This article explores the different degrees to which these three jurisdictions have gone beyond regulatory protection and the common law to confer on investors statutory rights to compensation for market manipulation.

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I. INTRODUCTION

Market manipulation, in its very nature, interferes with the natural forces of supply and demand. To allow market manipulation to take place unchecked is, therefore, to countenance actions that undermine the very foundations of the price formation mechanism. Rules against market manipulation, therefore, constitute the basic infrastructure that support efficient and well-functioning markets. The case for public regulation and enforcement seems fairly evident and indeed (as will be seen) the regulatory rules against manipulation in the U.K., Australia and Singapore have moved steadily toward formulations that ease the burdens of prosecution. Yet, the drive toward stronger regulatory protections against market manipulation does not necessarily translate into more robust private rights of action. This article explores the different degrees to which these three jurisdictions have gone beyond regulatory protection to confer on investors rights against market manipulation.

The natural starting point is the common law, for it is the limitations of the common law that prompt statutory innovations. To what extent has the common law been robust in combating market manipulation? Loss & Seligman have a fairly sanguine assessment of the response by the common law to the problem of market manipulation.\(^1\) My view is somewhat less sanguine. A doctrinally sound analysis of the cases that are often cited to demonstrate the common law’s protection of the concept of free and fair markets will reveal that the common law has played a somewhat more limited role in combating market manipulation. In Part IIA, I examine the doctrinal premises of \textit{R v Berenger}\(^2\) and underscore the fact that, apart from recognizing the concept of a free and fair market, the common law did not proscribe interference with a free and fair market as such. And insofar as treatment of contracts tainted by market manipulation is concerned, the refusal to enforce such contracts invariably stems from their illegality viz. they involve either a common law crime or infringe some statutory prohibition. The common law has not refused to enforce contracts because of an independent head of public policy based on its repugnance to interference with free and fair markets. The limitations of the common

\(^2\) (1814) 3 M & S 66, 105 ER 536.
law throws into sharp relief the critical importance of statutory rules for proscribing market manipulation, statutory rules which at the same time provide the bases by which to ascertain whether contract said to be tainted by market manipulation should be refused enforcement.

Securities pricing is determined by information, whether this be information concerning the issuer of the securities or information relating to risks attaching to the income stream expected from the security. The case for prohibiting market manipulative statements is thus fairly obvious. However, the self-evident case for prohibiting market manipulative statements does not necessarily translate also into the law conferring on investors rights to claim compensation for market manipulation. Undeniably, the common law on misrepresentation does potentially confer on investors some measure of protection against losses arising from market manipulative statements. That protection is, unfortunately, limited by the doctrinal premises of the law on misrepresentation. This is examined in Part IIC. In Part IIIA, a comparative study of the rules against market manipulation in the U.K., Australia and Singapore is undertaken to see how far statutory developments have carried the agenda of investor protection in this jurisdictions. We will observe how Australia, Singapore and the U.K. have responded somewhat differently to the recognizing investors’ right to compensation for losses from market manipulative statements. Australia has conferred on investors substantive rights to market integrity that are arguably wider than that found in US federal securities law – an interesting development bearing in mind that it was US federal law which was the inspiration for the earlier drafts of securities industry law in Australia. While Singapore securities law has ironed out the principal kinks to realizing investors’ right against market manipulation, I will show how investors’ rights continue to be fettered by an unfortunate restriction.

I then address the issue of market manipulative conduct in Part IIIB in which I examine the adoption of objective definitions that attempt to dispense with the requirement for proving mens rea. I argue that there is an irreducible relevance of motivations despite the

attempts at objectifying the elements of market manipulation. These attempts do not dispense with what is in essence an exercise in sifting legitimate behaviour from illegitimate behaviour. And insofar as a particular market moving conduct is capable of an innocent explanation, it is the motivations of the trader that impart to the conduct the quality of illegitimacy. I assess the impact of this theory on investors prosecuting their rights and consider how the trader’s legitimate interest against nuisance suits might be balanced against a legal system’s attempt at creating efficacious investors rights.

II. COMMON LAW ‘PROTECTION’ AGAINST MARKET MANIPULATION

A. Market manipulation and common law crimes

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This section argues against the view that the common law historically proscribed market manipulation and that a doctrinally sound view needs to distinguish the doctrinal device by which to attack market manipulation (i.e. through the crime of conspiracy to defraud) and the effect of the proscription (only conspiracies to defraud through market manipulation came within the ambit of the crime, not individuals acting alone).

It should be noted that the criminal law of Singapore was codified in 1871 before the founding of the stock exchange in 1960: Penal Code of the Straits Settlements (passed by the Legislative Council of the Straits Settlements in 1871, took effect from 16 September 1872). Interestingly, the two provisions relating to conspiracy (sections 120A and s 120B) were inserted in 1913. Codification of criminal law was carried out early on in the Australian states of Queensland (1899), Western Australia (1902) and Tasmania (1924). In Victoria and South Australia, the common law crime is expressly retained: see Crimes Act 1958 (Vic) s 321F(2) and Criminal Law Consolidation Act 1935 (SA) s 133(2). See further Bronitt & McSherry, Principles of Criminal Law (Sydney: Lawbook Co. 2005) p 426.
R v de Berenger is often cited as the *locus classicus* for the common law’s early response to market manipulation. Certainly, de Berenger’s blatant lies relating to Napoleon’s death and the allies’ conquest of Paris were calculated to increase the price of British government bonds. Nonetheless the case did not found a new crime of market manipulation. In English criminal law, it is properly characterized as a case of criminal conspiracy. De Berenger was charged along with other members of the British aristocracy who participated in the scheme. The crime in *R v de Berenger* was conspiracy to defraud; it does not create a crime of manipulation. As such, an individual who acts alone in manipulating the market falls outside the ambit of the case. The significance of the case lay more in the prosecution not having to allege that particular purchasers had suffered loss as a result of the actions. The ratio of *R v de Berenger* consists of the holding that the criminal conspiracy is constituted by the use of wrongful means for a wrongful purpose. Here, the wrongful means is located in the false rumours, and the wrongful purpose in the creation of an inflated value of the government security. Rather than founding a new crime of market manipulation, *R v de Berenger* is more a

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5 (1814) 3 M & S 66, 105 ER 536. See also *R v Aspinall* (1876) 1 QBD 730, affirmed (1876) 2 QBD 48 (Court of Appeal). Loss & Seligman characterize *R v Aspinall* as a criminal tampering with a public market:

[R v Aspinall involves a] conspiracy to obtain an exchange listing by false representations concerning fictitious allotments and amounts paid is a criminal tampering with a public market, even without allegation that purpose was to injure public traders by inducing them to buy shares that were valueless or worth less than they appeared to be. (Loss & Seligman, *Securities Regulation* (Aspen Publishers. 2004) Vol. XIII §3986.12)

Again, this would appear to overstate the ambit of the case. The defendants were charged on two counts of conspiracy. First, that the defendants had by false representations induced the Committee of the Stock Exchange to grant a settling day and permit the shares of the company to be quoted. Cockburn CJ was strongly of the opinion that the averment was insufficient to sustain conspiracy, while Blackburn and Field JJ declined to express an opinion as to its sufficiency. All three judges in the Divisional Court were, however, agreed that the Second Count was sufficient only because it also averred that the object of the conspiracy was to induce “persons who should thereafter buy and sell the shares to believe that the company was duly formed and constituted, and had complied with the rules of the Stock Exchange so as to entitle the company to have their shares quoted in the official list.” Rather than an abstract notion of tampering with the market, a careful study will show that an accurate characterization of the case leads one back to conspiracy to defraud member of the investing public. The underscored portions of the quotation above are therefore inaccurate; the three judgments clearly placed importance on the averment that the conspiracy involved deceiving members of the public.


7 Wai Yu-Tsang v R [1992] 1 AC 269. The essence of criminal conspiracy is ‘an agreement to practise a fraud on somebody.’
demonstration of how English common law of crimes fashioned the law of criminal conspiracy to address an instance of market manipulation.⁸

Loss & Seligman says the case establishes the concept of a free and open public market – and indeed the case does show the judges to be animated by such a norm.⁹ Nonetheless, one should not attribute greater significance to the case than is warranted. The case was not the acorn from which the crime of market manipulation sprouted. To the contrary, its uncertain scope has been more a cause for dissatisfaction¹⁰ and calls for its reform.¹¹ It remains, however, fair to say that through the crime of conspiracy to defraud, the common law demonstrated its antipathy toward attempts at manipulating prices in open

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⁸ Once it is appreciated that R v de Berenger is doctrinally located in the crime of conspiracy, the extension of wrong means from words to acts is only a matter of natural progression. As such, Scott v Brown, Doering, McNab & Co should not be attributed greater significance than it deserves. Though characterized as an example of how the common law reached market manipulative actions, its ambit is very much about agreements to effect market manipulative actions. Market manipulative acts are not per se reached by either R v de Berenger or Scott v Brown, Doering, McNab & Co.


¹⁰ The Law Commission, Criminal Law Conspiracy to Defraud, Working Paper No. 104 p. 71. The modern definition of conspiracy to defraud is found in Scott v Metropolitan Polite Commissioner [1975] AC 819. It suffices if two or more enter into “an agreement… to deprive a person of something which is his or to which he is or would be or might be entitled…[or] dishonestly to injure some proprietary right of [the victim]” (at p.840). It is not necessary to show that the victim was in any way deceived. The objection stems from the uncertain boundaries of the offence” and the “insufficient guidance as to what can or cannot lawfully be done and consequence infringe the principle that criminal law should be knowable in advance of the conduct to be penalized.” Law Commission WP No. 104 para 5.8. For a recent critique and attempt at reform, see Law Com No 276, Fraud (2002) Part III.

markets. One should hasten to add that the antipathy toward manipulation did not extend to proscribing attempts at manipulation not involving conspiracies.

B. Market Manipulation and Contracts

Loss & Seligman cite Scott v Brown, Doering, McNab & Co\textsuperscript{12} as an instance of “manipulation by trading alone”.\textsuperscript{13} A closer look at the case will reveal that the doctrinal basis of Scott v Brown remains firmly in the realm of conspiracy to defraud, though the issue which arose was one involving contract law. In Scott v Brown, the plaintiffs and their stockbrokers entered into an agreement wherein the latter would maintain the post-issue price of the shares at an agreed level. This was for the purpose of encouraging other investors to take up the shares. The plaintiffs sued to rescind their contract with the stockbrokers for purchase of shares. The court found that the purpose of the contract “was to impose upon and to deceive the public by leading the public to suppose that there were buyers of such shares at a premium on the Stock Exchange, when in fact, there were none but himself…”\textsuperscript{14} It was an illegal agreement. The claim to rescind the contract thus attracted application of the maxim “ex turpi causâ non oritur actio”.\textsuperscript{15} Accordingly the plaintiff’s claim for rescission was not failed.

The doctrinal basis of Scott v Brown was not the illegality of manipulative conduct. All three judgments relied on the illegality of the agreement, which revealed a criminal conspiracy to defraud. Without criminal conspiracy to defraud as a basis, it is questionable whether the manipulative conduct constitutes a category of public policy which attracts application of the ex turpi causa maxim.

\textsuperscript{12} [1892] 2 QB 724. Interestingly, there is a recent Singapore case whose facts bears a striking to Scott v Brown, Doering, McNab & Co is Irawan Darsono v Ong Soon Kiat [2002] 4 SLR 84; [2002] SGHC 133 (Plaintiff, who was interested in acquiring a substantial stake in the Defendant’s company, was asked by the Defendant to purchase the shares in the stock market at above the contracted price – with the promise that the Plaintiff will be indemnified to the extent of the difference between the market transacted price and the agreed price. The Defendant was convicted for creating a false or misleading market price under s 97 of the Securities Industry Act (Singapore, Cap 289) (now Securities and Futures Act section 197). The Plaintiff’s claim for the indemnity was dismissed as it is founded on an illegality.)

\textsuperscript{13} Supra n 9.

\textsuperscript{14} Ibid at 728-729, per Lindley LJ.

\textsuperscript{15} In English, the principle is aptly summarized in Lord Mansfield’s dictum in Holman v. Johnson (1775) 1 Cowp. 341, 343: "No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act."
Judicial antipathy toward market manipulative conduct has not develop into a distinct head of public policy by which to apply the *ex turpi causa* maxim. In *Fame Decorator Industries Pty Limited v Jeffries*, a former chairman of a company who held convertible preference shares sold large amounts of the common shares prior to the close of trading. This caused the shares which normally traded between 25c and 35c to fall to 14c and 13c. Such conduct was found to contravene sections 995 and 998 of the Corporations Law. Accordingly, the New South Wales Court of Appeal construed the terms of conversion to have an implied term that prices which were the result of illegal conduct were to be excluded from the computation. Given that the illegality of the conduct was in issue, alternative reasoning based on implied terms could have been used viz. it must be an implied term of the contract that prices distorted by an interested party would be excluded. That the court did not choose to adopt this as an alternative ground points to the difficulty of ‘interference with free market forces’ as a legal basis for adjusting contractual obligations. If antipathy toward attempts at creating an artificial market animates judicial willingness to interfere with contractual obligations, it has proceeded through the established ground of illegality, not as an independent ground of public policy.

Illegality, then, has been the interface for the interaction between market manipulative conduct and contractual rights. Illegality – by which is meant proscriptions backed by penal sanctions - has historically been the basis by which courts ascertain whether market manipulative conduct affect contractual rights. That being so, the way in which a statutory proscription is formulated plays a critical role in determining whether and how contractual obligations are affected by the market manipulative conduct.

**C. Market Manipulation and Torts**

Like common law crimes, the role of tort law in protecting investors against market manipulation has also been less than holistic. Investor compensation for fraud has primarily to rely upon the tort of deceit. In its nature, deceit involves fraudulent representations and statements. In the context of business investments, the example that

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readily comes to mind is one in which an investor is induced to purchase a large stake in a company by reason of a false representation about its operations and financial affairs; by and by, the investments come to grief when the true state of affairs comes to light. In the securities market, manipulators might issue baselessly optimistic comments on internet chat rooms about the financial or operational health of the issuer to ratchet up the traded price of a stock. Alternatively, the company itself might, in response to a developing scandal, issue false statements to maintain the trading price of its stock. In such instances, it is conceivable that investors who have bought at a higher price can claim under the tort of deceit.

Nonetheless, it is by no means an easy matter to sustain a fraud claim. Fraud is very much identified with dishonesty viz. the maker of the statement does not believe that the statement is true. One thus needs to have evidence to show that the maker of the statement was consciously aware that the statement was untrue when it was made. *Derry v Peek*, the *locus classicus* on the tort of deceit, illustrates the difficulties with the claim. Here, the directors were sued for inaccurate statement. Rejecting the notion that the directors should be liable for negligent statement found in the prospectus, the House of Lords ruled that it was only upon the proof of fraud that the investors could claim for their losses against the directors. The claimants bore the burden of showing that the directors did not honestly believe in the truth of the statement when they made it. Lacking such evidence, the claim predictably failed. Thus, unless a claimant has evidence that the defendant did not honestly belief in the truth of the statement at the point it was made, the claim is likely to fail. Applied in the context of accounting manipulation where there might be room for differential treatment of earnings recognition, the claimants do not necessarily have a claim even when there is an earnings restatement demanded by an auditor, it being arguable that the matter is one of professional misjudgment.

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17 (1889) 14 App Cas 337
18 The decision caused an uproar was statutorily reversed by the Directors’ Liability Act 1890 (UK), 53 & 54 Vict c 64
The second difficulty with the tort of deceit lies in the requirement that the statement be addressed to the injured claimant before he is entitled to make a claim. Historically, this element in the tort of deceit was used as a control against the potentially crushing claims of investors on the secondary market against directors of listed companies. It is true that in 1859, the Court of Exchequer in *Bedford v Bagshaw*\(^{19}\) allowed a claim by investors who claimed that the directors had, by a misrepresentation to the Council of the Stock Exchange, obtained a listing of worthless shares. In the view of Pollock CB, “[a]ll persons buying shares on the Stock Exchange must be considered as persons to whom it was contemplated that the presentations would be made.”\(^{20}\) The flicker of liberality was quickly snuffed out by the House of Lords in *Peek v Gurney*,\(^{21}\) which held that investors on the secondary market did not have any claim against directors for misstatements in the prospectus. The proximity requirement thus cuts down the class of persons who, though injured, might lodge a claim for compensation. At its narrowest, a misleading disclosure for compliance purposes is not addressed to investors even though the company may be aware that investors might rely on it. Unless a court finds that the maker of the statement intends also to address the plaintiffs, market players who rely on the disclosure will not have a claim. Others who rely on the integrity of the price formation process of the public markets will have even more difficulty lodging a claim. Amongst these will be the holder of convertible securities who, by reason of the artificially inflated prices, receives fewer shares under the conversion formula than if the prices had not been manipulated.\(^{22}\) Such investors fall outside the scope of the tort of deceit, which seeks to protect persons to whom fraudulent statements are addressed.

The reliance element in the tort of deceit requires the claimant to demonstrate that he has acted upon the misrepresentation. At first glance, it is an unimpugnable requirement – for it would appear strange that, without acting upon the misrepresentation, the claimant can sue the representator. Transposed onto an information sensitive market where investors expect integrity in the price formation process, the element becomes a stumbling block to realizing such investor interest. The practical implication, then, is that

\(^{19}\) (1859) 4 H & N 538 (Ex); 157 Eng Rep 951
\(^{20}\) (1859) 4 H & N 538 at 548 (Ex); 157 Eng Rep 951 at 956.
\(^{21}\) (1873) LR 6 HL 377.
\(^{22}\) This scenario is the flipside of *Fame Decorator Industries Pty Limited v Jeffries*, supra n 16.
investors who transacted at the manipulated prices are only able to claim if they knew of the statement and acted upon it. For those who merely relied on the integrity of the price formation process without more, their claims fail by reason of the lack of specific reliance. One does not have a claim merely because of the price distortion produced by the manipulation; one needs to show that one has relied on the statements or acts that generated the price distortion. Here therefore is where the tort of deceit does not map investors’ interest in a fair and efficient market. It is probably unfair to fault the tort of deceit for failing to do so; after all, its purport is provide redress for injury directly arising from fraudulent statements. What this points to, however, is the imperative of developing a statutory tort which more directly protects investors’ interest in the integrity of the price formation process in the market.

The need for such a statutory tort is accentuated by market manipulative conduct, which is caught by the tort of deceit only incidentally. The difficulty with catching market manipulative conduct under the tort of deceit lies in this: deceit is fundamentally about representations. It targets purposeful transmission of fraudulent messages. Conduct, in its nature, tends to be more ambiguous in the message it conveys (if there is one at all). Take the instance of one bidding up the price of a stock. Is any message intended? Is it not possible to argue that the message is merely incidental to the conduct? In other words, at issue is first the fundamental question of whether there is a representation, and secondly, whether the injured party is an intended recipient of the message. In theory, it is possible to characterize conduct as a representation; however, pinning market manipulative conduct down as a misrepresentation is probably practicable only where the message conveyed is clear in its context. Absent that, the theoretical possibility of conduct amounting to a misrepresentation does not readily translate into effective protection for investors injured by market manipulative conduct. The market manipulator may hide behind the difficulty of penetrating the mixed messages conveyed by his conduct. Market manipulative conduct that does not involve any intended representation will not be caught by the law on misrepresentation. A market squeeze or corner is market abuse by reason of one’s cornering the supply of the commodity, less a matter of misleading messages. Such market manipulative conduct is, from a conceptual
perspective, arguably outside the realm of misrepresentation. This highlights again the imperative of developing a tort which more specifically targets the ill of market manipulation.
III. MARKET MANIPULATION AS A REGULATORY OFFENCE AND AS AN ACTIONABLE WRONG

From Part IIA, we see that the common law protects investors against market manipulation only incidentally. *R v de Berenger* was not so much about proscribing interference with the operation of a free and open public market (though undoubtedly the case did have that effect); more accurately, it is about how the crime of conspiracy was adapted to apply to an instance of market abuse. As to the impact of market manipulative action upon the private law of obligations, we saw that contracts were affected only insofar as the action was affected by the illegality of the market manipulative action. Much therefore rests upon whether the market manipulative conduct is a crime, proscribed either at common law or by statute. The consistent strand of common law reasoning in cases dealing with market manipulative conduct emphasizes the need to locate the crime before the contract is affected.\textsuperscript{23} Importantly, market manipulative conduct (or a *specie* of it) has not – and does not – constitute a head of public policy at common law by which the courts consider a contract void or unenforceable. Doctrinally, a court’s refusal to enforce a contract must be located in the illegality of the action. We also saw the limitations of the law on misrepresentation as an avenue through which investors are provided a right to compensation for market manipulation.

In this section, we shall examine how statutory developments have overcome the limitations of the common law to establish a more robust regulatory framework – and importantly, how the UK, Australia and Singapore have responded differently to the inadequacies of the common law in providing investors with compensation rights for market manipulation.

A. Market manipulative statements

Common to both deceit and negligent misrepresentation is the element of specific reliance i.e. a representee must demonstrate the he has acted in reliance on the

\textsuperscript{23} Merely because statute proscribes particular conduct does not mean that the associated contract will be unenforceable. The courts need also to be convinced that the statute intends this result: *Aldrich v Norwich Union Life Insurance Co Ltd* [1998] CLC 1621(Breach of UK Financial Services Act s 47 held not to have an impact upon contractual obligations.)
representation. As such, if a misleading statement has been disseminated onto the market which raised the price of the security traded, the representee must demonstrate that he knew of the statement and embarked upon some course of action that is attributable to that statement. The mere fact that he has bought at a higher price than he would have in the absence of the misleading statement does not entitle him to claim compensation for the price difference. The requirement for specific reliance establishes the chain of causation between the wrong perpetrated and the damage suffered. If it is shown that an investor was motivated by other considerations and would have entered the transaction at that price level anyway, the cause of the damage is not attributable to the misrepresentation. Rather, the cause of the transaction would be these other motivating causes. Under the common law, the market manipulative statement would not be causally related to the damage suffered by the investor. *A fortiori*, an investor is unable to claim under the law of misrepresentation if he did not know of the misrepresentation and had merely ‘relied’ on the integrity of the information being disseminated onto the securities market.

In the U.S., the reliance element in Rule 10b-5 has moved from such specific reliance to a general reliance in the form of the ‘fraud on the market’ theory. The ‘fraud on the market’ theory creates a presumption that traders rely on the statements or omissions by reason of how the market operates:

The fraud on the market theory is based on the hypothesis that, in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business.... Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements.... The causal connection between the defendants' fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations.24

The theory was adopted by the U.S. Supreme Court in *Basic v Levinson* to create a presumption of reliance:

Presumptions typically serve to assist courts in managing circumstances in which direct proof, for one reason or another, is rendered difficult. ... The courts below accepted a presumption, created by the fraud-on-the-market theory and subject to rebuttal by petitioners, that persons who had traded Basic shares had done so in

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24 *Peil v. Speiser*, 806 F.2d 1154, 1160-1161 (Court of Appeals, 3rd Circuit. 1986)
reliance on the integrity of the price set by the market, but because of petitioners' material misrepresentations that price had been fraudulently depressed. Requiring a plaintiff to show a speculative state of facts, i.e., how he would have acted if omitted material information had been disclosed, see Affiliated Ute Citizens v. United States, 406 U.S., at 153-154, 92 S.Ct., at 1472, or if the misrepresentation had not been made, see Sharp v. Coopers & Lybrand, 649 F.2d 175, 188 (CA3 1981), cert. denied, 455 U.S. 938, 102 S.Ct. 1427, 71 L.Ed.2d 648 (1982), would place an unnecessarily unrealistic evidentiary burden on the Rule 10b-5 plaintiff who has traded on an impersonal market. ... Arising out of considerations of fairness, public policy, and probability, as well as judicial economy, presumptions are also useful devices for allocating the burdens of proof between parties... The presumption of reliance employed in this case is consistent with, and, by facilitating Rule 10b-5 litigation, supports, the congressional policy embodied in the 1934 Act. 25

Such a change to the doctrine of deceit and negligent misrepresentation at common law is remote in the utmost. 26 Any such change would have to take the form of statute. This indeed is the effect of section 199(1) of the Securities and Futures Act (Sing.):

No person shall make a statement, or disseminate information, that is false or misleading in a material particular and is likely —
(a) to induce other persons to subscribe for securities;
(b) to induce the sale or purchase of securities by other persons; or
(c) to have the effect of raising, lowering, maintaining or stabilising the market price of securities,

if, when he makes the statement or disseminates the information —
(i) he does not care whether the statement or information is true or false; or
(ii) he knows or ought reasonably to have known that the statement or information is false or misleading in a material particular.

Under section 234 of the Securities and Futures Act (Sing.), a contemporaneous trader may institute a civil claim if he has suffered loss by reason of the difference between the price at which the security was traded contemporaneously with the contravention, and the price at which the security was likely to have traded if the contravention had not occurred.

26 It must be acknowledged that there have been valiant attempts at arguing for fraud on the market at common law. See, for example, Yadlin, “Fraud on the Market at Common Law: Lessons from Contemporary Finance and Economics”, (2000) 2 ICCLJ 59.
A right in the nature of s 234 read with s 199 has important theoretical underpinnings. It goes beyond the common law of deceit which recognizes one’s compensatory interest only to the extent that one has acted in reliance on the misleading statement. It dispenses with the causation logic that undergirds the law of misrepresentation at common law. Implicitly, it embraces the fraud on the market theory by creating a right to compensation where the price has been distorted by false or misleading statements. The nature of the investors’ protected interest thus changes as one moves from the common law of deceit and negligent misrepresentation to the statutory action founded on s 199. From the protection of one’s reliance interest in statements given for one’s consumption, the investor is now accorded a compensable right to the integrity of the information being disseminated onto the securities market.

The Australian provision conferring on investors the right to sue for breach of the equivalent Australian proscription (Corporations Act s 1041E) is not as explicit. Section 1041I of the Corporations Act merely says:

A person who suffers loss or damage by conduct of another person that was engaged in in contravention of section 1041E … may recover the amount of the loss or damage by action against that other person or against any person involved in the contravention …

The statute does not elaborate on when one ‘suffers loss or damage by conduct of another person’. In respect of fraudulent or negligent statements, must it be demonstrated that the claimant acted in reliance on the statements? The Australian legislation does not explicitly address this issue. The better view is that there is no such requirement. This, for a number of reasons. First, section 1041E essentially reproduces the constituent elements of fraudulent and negligent misrepresentation. If the legislature intends for the right to private remedy in s 1041I to incorporate the specific reliance element, it could have done so. This was the case in the Directors Liability Act 1890 (UK), where the statutory language posits reliance. The omission is therefore telling. It is indicative of the legislature intending that the elements of the action be somewhat different from the

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27 A director is liable to all persons who shall subscribe for securities “on the faith of” prospectus or notice inviting subscriptions for such securities for “the loss or damage they may have sustained by reason of any untrue statement in the prospectus or notice…”: section 3 of the Directors’ Liability Act 1890 (UK), 53 & 54 Vict c 64. Later Companies Act 1948 (UK) s 43.
common law action. Moreover, there is no reason for the legislature to reproduce in statutory form a cause of action that exactly maps the elements of the common law action. Second, the formulation “by conduct [of the contravenor]” posits the need to show “some sufficient cause or reason linking the conduct with the recoverable loss or damage”. Section 82 of the Trade Practices Act (Aust) (“TPA”) is framed in terms similar to section 1041I of the Corporations Act. Australian case-law acknowledges that the common law notions are merely *prima facie* rules which may be displaced or modified according to the purposes sought to be achieved by the statute. In *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd*, the Federal Court of Australia held that a business rival could claim civil compensation under TPA s 82 for contravention of TPA s 52 even though he did not rely on the representation. The defendants had made representations which arguably constituted “misleading or deceptive conduct”. The plaintiffs sought to argue that the representations induced pharmacists and the public to purchase the defendant’s drug rather than the plaintiff’s drug, “thereby causing the [plaintiff] to lose sales of its drug Vermox which it would otherwise have made and continued to make …” Lockhart J rejected the defendant’s argument that s 82 precluded a person who had not relied on the representation making a claim under the section:

> Section 82(1) should not be given a restricted meaning to be available only to the person who suffers loss or damage by reason of his own reliance upon the representations which constituted the relevant contravention of Part IV or V; nor for that matter should it be given an extended meaning which strains the language used by the legislature. But a person who suffers damage by reason of or as a result of the conduct of the contravener (albeit that that person does not himself rely upon the representations) is not to strain the language of the subsection, but to interpret it according to its ordinary and natural meaning. For a person to recover under the section he must suffer loss or damage by reason of or as a result of the contravention. There is nothing unduly wide about that..

This line of argument should also apply to CA s 1041I given the similarity in statutory language. If it is accepted that the theoretical basis of CA s 1041I lies in according to

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29 (1992) 109 ALR 638 (Federal Court of Australia)
30 Amended statement of claim para 23A: ibid at p 639.
31 Ibid at p 643-644.
interested persons a protected interest against market distortion, it should be open to an aggrieved party to argue that by reason of the contravention, the price was at a higher level that he otherwise would have purchased the security - and thereby link the wrong to his loss.

From a theoretical perspective, it can fairly be argued that the investor in Australia and Singapore now has a compensable right to the integrity of the information being disseminated onto the securities market. The significance of this shift from the narrower reliance-based compensatory interest underpinning the law of misrepresentation to a broader right against market-distorting statements has significance beyond the theoretical basis inspiring the private right of action. Potentially, the shift also smoothes the way for class or group action by investors. The elements of the proscribed conduct are common to all potential claimants. The issues specific to investors would be: (i) who qualifies as contemporaneous traders, and (ii) the loss suffered by the contemporaneous trader. The removal of specific reliance removes the need to prove the causal connection between the misstatement and one’s entering the transaction. The removal of this evidential obstacle also obviates the time- and cost-consuming exercise of litigating out this element for each individual investor. The cost of the class or group action falls accordingly. Who constitutes contemporaneous traders or similarly situated members of a class can be dealt with by a ruling on its parameters. Moreover the loss suffered should be one that is susceptible to ready quantification by reference to the difference between the price with the market manipulative statement and the price without the market manipulative statement.

In contrast to the statutory developments in Australia and Singapore, the rights of investors under U.K. law remain largely a matter of the general law. This should not, of course, be taken to suggest that the regulatory law has not developed; to the contrary, there is a very sophisticated regime of market abuse rules in the U.K.\textsuperscript{32} What is perhaps noteworthy is that the developments in regulatory rules have not been closely followed by conferring on investors equally wide rights to sue for their breach. From the perspective of an investor’ compensatory interest, then, his rights under U.K. law has not

\textsuperscript{32} See text to n 56 -60.
progressed to a broader protection of his interest in the integrity of information feeding the price-formation process, as has taken place in Australian and Singapore law. It remains very much anchored in common law framework of protecting his reliance interest in statements directed at him.

B. Market manipulative conduct

As has earlier been discussed, while manipulative conduct can conceivably be caught by the law on misrepresentation, conduct which conveys no clear message falls outside the ambit of misrepresentation. An investor injured by a market squeeze has little recourse. Similarly one prejudiced by the distorted price generated from a large buy order at the close of trading. From a regulatory perspective, neither of these two instances of market manipulations will be caught by the law on conspiracy to defraud unless there is more than one party involved in the manipulative scheme.

Is the case for a statutory proscription against manipulative conduct an uncontestable one? Further, is the case to confer on the investor a statutory right of action for manipulative conduct demonstrably worthy of having on the statute books?

1. Fischel & Ross’s challenge to anti-manipulation law

In the context of U.S. federal securities law, Fischel & Ross have in a 1991 article cast doubt on the need for a specific proscription against market manipulation. Their arguments were framed in the context of US securities regulation, where manipulation is nowhere defined in the legislation. The courts are therefore left to work out the ambit


34 Ibid at p 507-510. Their principal focus is upon ‘manipulation’ in the form of buying a security in order to increase its reported price or selling a security to decrease its reported price, which arguably fall within the ambit of section 9(a)(2) of the Securities Exchange Act and rule 10b-5.

The Securities Exchange Act 1934 has a number of provisions that target specific forms of manipulation. For example, s 9(a)(1) proscribes wash sales and matched sales, s 9(a)(3) targets the circulation of information by broker-dealers (and others attempting to market or purchase securities) to the effect that a price movement is imminent because of the activities of certain traders, s 9(a)(4) proscribes the making of false or misleading statements for the purpose of inducing others to trade while s 9(a)(5) adds to s 9(a)(3) by prohibiting others from doing on behalf of broker-dealers etc that which s 9(a)(3) prohibits. Fischel & Ross have little issue with manipulative conduct like wash sales and matched sales, which they
of the concept. Fischel & Ross contend that the law on manipulation in the US context is otiose, because that which should be proscribed is already covered by the concept of fraud. Manipulative statements, they argue, should properly be characterized as a specie of fraud. Wash sales and matched orders are seen as species of conduct-based fraud. To the extent that these are covered under the concept of fraud, their characterization as manipulative is duplicative and unnecessary.

To Fischel & Ross, the law should not proscribe ‘manipulation’ in the form of buying a security in order to increase its reported price or selling a security to decrease its reported price. Herein lies the sting in their overarching thesis that the concept of manipulation should be abandoned together. Fischel & Ross argue first that successful manipulation is unlikely. Second, that the opacity and breadth of the broadly framed anti-manipulation provisions do not adequately discriminate legitimate activities from illegitimate ones, and therefore that the law risks dampening socially beneficial activities. The authors argue that whereas crimes are typically identified by harmful outcomes, ‘no objectively harmful act or bad outcome’ is associated with trade-based manipulation. They argue that purely objective tests are inadequate to capture the evil that an anti-manipulative rule targets. For example, the identification of manipulation with the notion that one is interfering with demand and supply does not lead one very far. After all, one’s very involvement in the securities market contributes toward the forces of demand and supply. “Interference” is meaningless unless one has a conceptual device by which one determines what is or is not interference. Similarly, the notion of artificial prices calls for a conceptual delineation of the “natural” on the one hand and the “unnatural” or

characterize as a specie of fraud: pp 510 - 512. (They cite Scott v Brown, supra n 12, as authority. As has been argued in this article, the illegality in Scott v Brown is properly characterized as a conspiracy to defraud.) Neither do Fischel & Ross have issue with statement based manipulation, which they also characterize as a specie of fraud: ibid at pp 510 - 512.

36 Ibid at pp 510 – 512.
37 Ibid at pp 510 - 512
38 Which arguably fall within the ambit of section 9(a)(2) of the Securities Exchange Act and rule 10b-5
39 I shall not revisit the refutations of this argument, which are sufficiently canvassed in the literature following publication of the article. See, for example, Steve Thel, “$850,000 in Six Minutes – The Mechanics of Securities Manipulation” 79 Cornell L Rev 219 (1994).
40 Supra n at p. 519.
“artificial” on the other. The authors suggest that ultimately, what manipulation boils down to is the intention of the person making the trade.

There is much that is problematic with Fischel & Ross’ thesis. While there is some truth to the notion that “it is extremely difficult to discern the intent of a trader with objective evidence”, objective evidence does not consist merely of the impact of the trade. In *Scott v Brown*, the intention of the trader was revealed by the agreement between the trader and company which reaped the benefit from the manipulation. In the Singapore civil penalty action against Frank Kuhn Swi Wha, the defendant had on four occasions purchased certain shares just before the close of trading in order to increase the price of the shares and thereby avoid margin calls.\(^{41}\) The motivations of the defendant were revealed in the course of investigations.

One can also take issue with the premise that there is no objectively harmful outcome in trade-based manipulation. The policy objective behind the prohibition is the prevention of price manipulation. In Frank Kuhn’s case, the closing prices of the shares conveyed a false impression of the market valuation. That the trades were not fictitious does not address why the law prohibits such market manipulative conduct.

Even if one grants that there is no harmful outcome from trade-based manipulation, the law on conspiracy, attempts and other inchoate crimes demonstrate that criminal law is concerned with more than harmful outcomes. Yet these are well established categories of criminal conduct. In prohibiting market manipulation, the law is (at its core) prescribing that one must not trade *for the purpose of* affecting the market-reported price.\(^{42}\)

Notwithstanding the problems inherent in Fischel & Ross’ thesis, their insight into the relevance of motivations is nonetheless a sound one. This, in my view, points to the

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\(^{41}\) MAS Press Release, “Civil Penalty Action for False Trading” (11 May 2006). The closing prices of ASA shares for the relevant dates were 13% to 23% above the prevailing market prices. Kuhn admitted to civil penalty liability under SFA (Sing) s 197(1)(b) and agreed to pay $50,000 to the MAS without court action.

\(^{42}\) *Marra v North* (1981) 148 CLR 42 at 59 (“By "genuine supply and demand" I exclude buyers and sellers whose transactions are undertaken for the sole or primary purpose of setting or maintaining the market price.”: Mason J)
'irreducible relevance of motivations’ even in objective formulation that appear to dispense with subjective mens rea requirements.

2. The irreducible relevance of motivations

To scholars and policy makers working outside the U.S. context, it is tempting to dismiss Fischel & Ross’ arguments as irrelevant. The definitional problems of ‘manipulation’ that Fischel & Ross discuss appear to be a peculiarly U.S. phenomenon. However, I would argue that if one looks at the objective formulations as demonstrated in the U.K., Australia and Singapore, ‘motivations’ continue be relevant in determining whether the ‘objective’ criteria are satisfied. Shorn of their more unpersuasive arguments relating to the self-deterring nature of manipulation and the difficulty of profiting from it, Fischel & Ross’ insight into the importance of motivations should be developed to provide safeguards for bona fide traders.

Their caution about the dangers of over-deterrence and the opportunity costs that attend foregone beneficial activity are apposite – though one might be skeptical about their prescription that the trade-based manipulation should not be prohibited. These risks counsel checks against over-zealous enforcement. They point also to the need for safeguards against potential harassment, whether by public officials or private litigants. They should prompt institutional check like parliamentary oversight and ombudsmen that might be employed to address complaints of investigatory harassment. In the private litigation context, the allowance for pre-trial discovery and interrogatories should not degenerate into ‘fishing expeditions’; rules relating to costs might also be employed to penalize vexatious proceedings. The irreducible relevance of motivations theory serves as an invaluable safeguard against harassment within the substantial definition of the offence.

There is, of course, room for the per se criminalization of certain kinds of market conduct. In Australia and Singapore, one’s participation in transactions involving no change in beneficial ownership is deemed to create a false or misleading appearance of
active trading on a securities market, and is hence an offence under SFA (Sing) s 197(1) and CA 2001 (Aust) s 1041B(1). Similarly deemed an offence is a transaction in which one or one’s associate acts as a counterparty for substantially the same quantity at substantially the same price – what might be termed “matched orders”. Such trades smack of a manipulative intent, but more than this, there is a good case for creating a presumption that such conduct amounts to manipulative conduct. Whether the presumption should be rebuttable is of course an issue of policy. The trader may be permitted a defence based on his innocent motivations, as is the position in Singapore. Under Singapore law, the presumption that there is false trading and market rigging from wash trades may be rebutted by the trader demonstrating that the “purpose or purposes for which he did the act was not, or did not include, the purpose of creating a false or misleading appearance of active trading in securities on a securities market.” Australia has gone further to delete this defence, so that traders found to have engaged in matched orders or wash sales are now irrebutably presumed to have committed an offence. Traders must therefore take precautions to avoid participation in such a transaction.

Beyond transactions which objectively smack of manipulation, the determination whether a trade is manipulative or not must surely depend on the intent of the trader. The mere fact that one’s transactions on the securities market resulted in a change in the price cannot be sufficient evidence of manipulation. The bid and ask price for a security are derived from the orders placed by all traders; that one’s orders have resulted in a change in the market price is an outworking of the price formation process. Anti-manipulation law is perhaps better seen as discriminating between legitimate and illegitimate trading. And insofar as the trading is not *ex facie* objectionable, the legitimacy and illegitimacy must surely depend on the intentions of the trader.

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43 SFA (Sing) s 197(3)(a); CA (Aust) s 1041B(2)(a). These are analogues to section 9(a)(1)(A) of the (US) Securities Exchange Act.
44 SFA (Sing) s 197(3)(b) and (c); CA (Aust) s 1041B(2)(b) and (c). The equivalent under the (US) Securities Exchange Act are sections 9(a)(1)(A) and 9(a)(1)(B).
45 SFA (Sing) s 197(4).
46 SFA (Sing) s 197(4).
47 See present CA (Aust) s 1041B. Before the amendment, the defence stemming from the purity of the trader’s motivations was available in a criminal prosecution, though not in a civil penalty action: *ASC v Nomura International* [1998] 1570 FCA (10 December 1998), discussing Corporations Law s 998.
This point is illustrated with an example. Suppose CD purchases a very large bloc of shares through a succession of orders. This necessarily moves the prices upwards. But the trading is not necessarily manipulation, for one may have very legitimate reasons for making the purchase. One may be building up a beachhead by which to make a takeover bid. Subject to reporting requirements, such stake-building prior to reaching the point where a mandatory offer is triggered is very much a feature of the takeover regimes in the U.K., Australia and Singapore. Thus, unless there are good reasons for prohibiting all manners of stake-building, anti-manipulation laws should not prevent such an activity.

Now suppose that the trader’s motive is not to acquire control, but merely to hold. Suppose further that the trader aims to gain collaterally from an OTC derivatives transaction, which settlement is based on the transacted price of the underlying security. Here, one might consider the trader to have crossed the line from legitimate trading to illegitimate trading. But even here, one has to grapple with the predictable argument by one so charged, that one’s principal aim was to make further investments and that the gain from the OTC transaction was an incidental collateral benefit. The lawfulness of the trade stands or falls by whether the trader’s motives are legitimate or illegitimate. It is the trader’s motive that helps one ascertain whether a trade is or is not manipulative.

3. Diminishing the \textit{mens rea} requirement but …

In the U.K., Australia and Singapore, the statutory formulations of market manipulation have moved steadily toward objective definitions that dispense with proof of a blameworthy state of mind. The proscription in CA (Aust) section 1041B (1) is illustrative:

A person must not do, or omit to do, an act … if that act or omission has or is likely to have the effect of creating, or causing the creation of, a false or misleading appearance: … (b) with respect to the market for, or the price for trading in financial products …

48 The Singapore provision is a similar: SFA (Sing) s 197(1). FSMA (UK) s 397(3) is stricter; the defendant’s act must “create a false or misleading impression as to the market in, or the price or value of … investments.” The distortion in the market must therefore be proven. Moreover, it must be proven that the defendant did the act “for the purpose of creating that impression”. Cf. The definition of market manipulation for the purpose of market abuse in FSMA (UK) s 118(5), which copies out the equivalent provision in Directive 2003/6/EC. See text to n 56-60.
A simple definition employing an objective test. Can one determine the artificiality of a price without regard to the motives of the trader? Is the price rise resulting from one’s acquisition of a substantial stake an artificial price merely because the price declines after one’s acquisition? What if one had in mind stake-building ahead of a takeover? What if one’s acquisition was in the hope of selling out upon the coming to pass of rumors that a takeover bid was impending?

The indispensable role of the trader’s motivations is seen in Donald and Australian Securities and Investments Commission. Donald was employed by ABN-AMRO as a dealer’s representative. The client, National Australian Asset Management (NAAM), was interested in acquiring a substantial position in Burswood. Donald misconstrued the authority to buy 500,000 shares and read the client’s intentions to mean a minimum acquisition to bring about a significant price rise. While giving instructions to ABN-AMRO’s operator of the Australian Stock Exchange Automated Trading System, he said he “want(ed) to give these Burswood’s a bit of a nudge upwards”. In his appeal before the Administrative Appeals Tribunal against the banning order issued by the ASIC, Donald was found to have contravened s 998(1) for creating trades that give a false or misleading appearance with respect to the price of Burswood shares. The Tribunal put much store on the fact that Donald’s orders brought the closing price to 95c where the stock had been trading at 89c. It is interesting, nonetheless, that there was no suggestion that the client, NAAM, was blameworthy for issuing instructions for such a large quantity to be bought. If Donald had not told the operator that he wanted to nudge the price upwards and had not expressed his views about the appropriate price of the stock but had merely carried out the client’s instructions, it is questionable whether there was a securities offence. What damned Donald was therefore his wanting to move the price, more precisely, his intention to move the price significantly with a lowest possible volume. Admittedly, Heeren J in an earlier appeal in the same case adopted the view that the mens rea element was a minimal one – the prosecution needs only show that the defendant intended to bring about the conduct, there is no need to show that he knew the conduct will bring about a false or misleading appearance in the market for the security.

49 [2001] AATA 366
It is certainly true that the statutory formulation admits of an objective test that permits conviction based on conduct that is likely to create to a false or artificial market. Nonetheless, the issue of whether a price is artificial cannot be solely determined by the new equilibrium brought about by the large volumes of one’s orders. There must be something blameworthy about these orders that result in a false or artificial market. That is, the false or artificial market is inextricably tied to the one’s motivations for giving the orders. The quality of the market – whether it is false or artificial – is informed by one’s motivation.

This argument is not at variance with the dicta of Heeren J in *Donald v ASIC*[^50] and Sackville J in *Nomura v ASIC*[^51] that the ‘likely to create’ limb of the offence dispenses with proof of a blameworthy intention on the part of the trader. It is not that the prosecution needs to prove *mens rea* in the form of an intention or knowledge that the trade is likely to result in a false or artificial market. The role of one’s motivations is somewhat more subtle. In essence, it informs the legitimacy or illegitimacy of one’s trade, ergo, whether there exists a false or artificial market.

The trader’s motivations serve to discriminate between legitimate and illegitimate transactions. Inevitably the trader’s motivations critically inform the issue whether the reported market price is or is not artificial. Whether or not there is an artificial price is difficult to determine apart from the trader’s motivations. Traders’ motivations inevitably play an important role in separating legitimate trading from illegitimate trading, one that is not buried by seemingly objectivity of phrases like “artificial prices”[^52] or “false or misleading signals”.[^53] Liquidity and indeed free operation of the market will be quite impaired if detractors can allege artificial prices merely by the significant movements resulting from one’s trades. It potentially supplies the ammunition by which opponents derail stake-building by a potential bidder. Indeed, interpreted so broadly, it is more likely to interfere with natural forces of demand and supply, rather than safeguard its natural workings.

[^50]: [2000] FCA 1142
[^51]: (1998) 89 FCR 301
[^52]: CA (Aust) s 1041A, SFA (Sing) s 197.
[^53]: MAD Article 1(2)(a)
There is undeniably a recent trend toward strict liability and objective formulations that dispense with onerous *mens rea* requirements.\(^{54}\) Australia’s Corporations Law 1989 s 997, which finds its inspiration in section 9(a)(2) of the (U.S.) Securities Exchange Act 1934, carried a fairly substantial *mens rea* element:\(^{55}\)

A person shall not enter into or carry out, either directly or indirectly, 2 or more transactions in securities of a body corporate, being transactions that have, or are likely to have, the effect of increasing the price of securities of the body corporate on a stock market, with intention to induce other persons to buy or subscribe for securities of the body corporate or of a related body corporate.

Its present incarnation – Corporations Act s 1041A – dispenses with the proof of an intention to induce others to trade:

A person must not take part in or carry out …a transaction that has or is likely to have … the effect of creating an artificial price for trading in financial products …

In the U.K., the objective anti-manipulative provisions came in the form of an add-on to existing provisions which are infused with intentionality elements. In a criminal prosecution for market manipulation by conduct under Financial Services Act 1986 s 47(2),\(^{56}\) for example, it must be proved that the defendant created:

“a false or misleading impression as to the market in or the price or the value of any investments… *for the purpose* of creating that impression and of thereby inducing another person to [transact in those investments]”. (emphasis mine).

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\(^{55}\) No. 109 of 1989. Cf. SEA (US) s 9(a)(2):

It shall be unlawful for any person, directly or indirectly, by the use of the mails or any means or instrumentality of interstate commerce, or of any facility of any national securities exchange, or for any member of a national securities exchange—…To effect, alone or with one or more other persons, a series of transactions in any security registered on a national securities exchange or in connection with any security-based swap agreement (as defined in section 206B of the Gramm-Leach-Bliley Act) with respect to such security creating actual or apparent active trading in such security, or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others.

\(^{56}\) c. 6. Repealed and re-enacted as Financial Services and Markets Act 2000 s 397(3). The prohibition against market manipulative conduct contained in s 47(2) of the Financial Services Act was new compared to the prohibition against market manipulative statements contained in FSA 1986 s 47(1) [now FSMA S 397(1)]. FSA 1986 s 47(1) traces its lineage to Prevention of Fraud (Investments) Act 1939 s 12(1) and Prevention of Fraud (Investments) Act 1958 s 13(1).
FSMA 2000 Part VIII introduced an administrative regime for “market abuse” where the equivalent provisions targeting market manipulation dispenses with the subjective *mens rea* element found in what was FSA s 47(2). One category of proscribed market manipulative conduct under the market abuse regime consisted of: \(^{57}\)

… *behaviour that is likely to give* a regular user of the market *a false or misleading impression* as to the supply of, or demand for, or as to the price or value of, investment of the kind in question…

The EU Market Abuse Directive \(^{58}\) necessitated a somewhat more nuanced objective approach, one that implicitly recognizes what present author terms the “irreducible minimum of intentionality” in constructing the notion of manipulative conduct. In 2005, the market abuse provisions received extensive revision to bring them into compliance with the U.K.’s EU obligations. \(^{59}\) Market manipulation by conduct is now predicated on: \(^{60}\)

Behaviour [that] consists of effecting transactions or orders to trade (otherwise than for legitimate reasons and in conformity with accepted market practices on the relevant market) which (a) give or are likely to give, a false or misleading impression as to the supply of, or demand for, or as to the price of, one or more qualifying investments, or (b) secure the price of one or more such investments at an abnormal or artificial price.

The move toward definitions that permit establishing market manipulative conduct through objective conduct criteria is doubtlessly driven by the desire to remove the obstacle presented by the difficulty of subjective intention. As I have sought to argue, the traders’ motivations will nonetheless continue to insinuate themselves into the

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\(^{57}\) FSMA s 118(2)(b) (repealed by The Financial Services and Markets Act 2001 (Market Abuse) Regulations 2005, S.I. 381/2005). The other - FSMA s 118(2)(c) - employed an equally objective formulation:

a regulator user of the market would, or would be likely to, regard the behaviour as behaviour which would, or would likely to, distort the market in investments of the kind in question.

\(^{58}\) Directive 2003/6/EC.


*Market manipulation shall mean: (a) transactions or order to trade: which give or are likely to give, false or misleading signals as to the supply of, demand for or price of financial instruments; or which secure, by a person or persons acting in collaboration, the price of one or several financial instruments at an abnormal or artificial level…*
objective definitions.\textsuperscript{61} The task for judicial interpretation lies in tackling the intention-informed legitimacy/illegitimacy divide that is inherent in the concepts of ‘artificial prices’ and “false or misleading market”. \textit{Ex facie}, definitions like CA (Aust) s 1041A and 1041B require the prosecution to establish why the prices or market is ‘artificial’.

Unusual trading activity might not necessarily mean that the prices generated thereby are ‘artificial’ or that there is a ‘false or misleading’ market; such will be the case where there is a desire to acquire a significant stake or to strongly signal one’s assessment of market over-valuation. Concepts like ‘artificial’ embed a value judgment on the legitimacy of the trader’s actions, which in turn point to the indispensable relevance of one’s motivations.

The indispensable relevance of one’s motivations to ascertaining legitimate from illegitimate trading has a number of ramifications. In a definition like that found in Australia’s CA s 1041A and s 1041B, it will be embedded in the concepts of ‘artificiality’, ‘false’ and ‘misleading’. Since the prosecution has presumptively to prove blameworthy conduct, conduct that is equally capable of innocent explanation should not be capable of sustaining a conviction. It might make a difference if the statutory formulation expressly acknowledges the relevance of one’s motivations. The definition of manipulating transactions in the EU Market Abuse Directive sifts out ‘legitimate reasons’ as an exculpatory element. The onus might thereby be on the defendant to show that he has legitimate reasons for his actions. The prosecution continues to have the burden of demonstrating that the market or price is at ‘abnormal level.’ Here perhaps, ‘abnormal level’ might be interpreted to mean unusual, given the room for the defendant to establish a defence based on the legitimacy of his motivations. The explicit provision of a defence based the relevance of motivations interestingly opens up room for a presumption of market manipulation from unusual trading.

Such a regulatory approach might arguably be justifiable for the ease with which regulatory enforcement action might be brought, though with it comes issues like whether speculation and momentum trading are considered legitimate. In the U.K., the Financial 

\textsuperscript{61} Except, of course, where in instances of wash sales and matched orders where per se proscription is possible.
Services Authority has sought to clarify the issue by a guidance in its Code of Market Conduct. MAR 1.6.7 states:

“It is unlikely that the behaviour of market users when trading at times and in sizes most beneficial to them (whether for the purpose of long term investment objectives,… or short term speculation) and seeking the maximum profit from their dealings will of itself amount to distortion.

It is important to note that this is not a safe-harbour, but merely an indication of how the enforcement agency views an activity like speculation. Cold comfort, perhaps, to momentum traders whose trades move the market, especially in less liquid stocks. If the matter does go to litigation, such speculators will probably have the burden of convincing the court that the trading counts as legitimate trading. The approach – the presumption of liability for market manipulation from unusual market movement – assumes the bona fides of the regulator who is only driven to call into account unusual market activity, and who is scrupulous in containing his regulatory enthusiasm so that the prosecutorial ease does not degenerate into having the effect of harassment.

4. Private rights of action piggy-back on regulatory proscriptions

An interesting facet in Australian and Singapore securities law is the creation of piggy-back civil rights of action that piggy-back on the regulatory proscriptions. A person whose conduct falls within the anti-manipulative provisions under Australian and Singapore securities law is also liable to compensate the investors for losses occasioned by breach of the regulatory proscriptions. The lower obstacles to regulatory enforcement translate also into a potential for harassment and attempts at extracting collateral benefits. The greater the ease with which such an action can be brought, the greater the nuisance potential of such lawsuits. A competitor might, by the right of private action, require that potential bidder account for his actions; and since there is an

62 This is contrasted with the position in the U.K. where there is no such express statutory right of civil action. In Aldrich v Norwich Union Life Insurance Co Ltd [1998] CLC 1621 and Norwich Union Life Insurance Co Ltd v Quershi [1998] CLC 1605, the courts found FSA s 47 not to create an implied right of (civil) action. It would also appear that contracts are unaffected by manipulative conduct contrary to FSA s 47 (now FSMA s 397). See Aldrich v Norwich Union Life Insurance Co Ltd [1998] CLC 1621, per Rimer J.
ex facie illegality, an injunction might issue in the meantime. Corporate insiders, through their shareholdings, might stymie hostile bidders and thus use the action for favouring their preferred white knight. Depending on the room permitted for discovery under the rules of civil procedure, one might using allegation of market manipulation seek to obtain information about a private investor’s related holdings and trading patterns. An investor who unloaded a large position might be called upon to provide further details that render more credible his claim that he sold because of his cash-flow needs. The presumption of market manipulation from unusual trading without more is capable of generating nuisance suits and strategic litigation. The potential for liability might very well drive out institutions with much to lose from such strategic litigation, and with that follows unfortunate knock-on effects for liquidity. The piggybacking of a civil claim upon a proscription that adopts such a presumptive approach to market manipulation is therefore fraught with dangers for the smooth functioning of the financial and capital markets. It may just be as well that section 118(4) of the UK FSMA is a purely regulatory provision that does not contemplate private rights of action.\(^63\) In the context of Australia and Singapore, rejecting the embeddedness proposition advanced above and interpreting the current provisions to mean liability premised on unusual activity would increase the potential for abuse of the private right of action. This lends additional weight to the argument that the current formulations have embedded in them the requirement that the prosecutor – and by extension, the plaintiff – prove the illegitimacy of the trading.

It cannot be that investors are permitted to sue merely because another’s trading has resulted in significant price changes. Conceptually, this does not locate the ‘wrong’ that one has suffered. Insofar as the action might (depending on one’s motivations) yet be legitimate, there is little room for adopting a presumption akin to ‘res ipsa loquitur’.

From a policy perspective, such an approach that requires legitimate traders to account to all who call them to account is undesirable, for it opens up the room for nuisance suits

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\(^63\) While FSMA 2000 s 150 confers on private persons the right to sue an authorized person for breach of rules that the Financial Services Authority creates for regulation of authorized persons, the Principles of Business and Code of Market Conduct are in the nature of Guidance under Part X Chapter II. The better view is that they are outside the ambit of FSMA 2000 s 150. Cf. Avgouleas, *The Mechanics and Regulation of Market Abuse: A legal and economic analysis* (London, 2005) p 394.

As to impact on contracts affected by breach of market abuse provisions, see FSMA 2000 s 131 (the imposition of a penalty does not render any transaction ‘void or voidable’.)
and suits for strategic advantage. And from the perspective of judicial construction, it is one to be eschewed in the absence of clear legislative intent for it to be so.

C. A ‘Puzzle’

It would be ironical for Commonwealth jurisdictions, who have long feared the American-style nuisance suits, to create a cause of action that paves the way for strategic and nuisance litigation. A puzzle that might come to mind is why there has not been a greater amount of securities litigation than observed.

One would venture to suggest that the answer is firstly to be found in litigation funding. The atomized claims of small investors makes it uneconomical for them to pursue litigation. Typically, the gains from litigation to these small investors are small compared to the cost of maintaining the litigation; they are thus individually non-viable claims. While there are procedures for aggregating common claims, there are further risks of liability from the “loser pays” rule in the event that the litigation fails. The problems arising from agency costs in the supervision of litigation process presents a further hurdle to potential litigants participating in the litigation. One institutional innovation that has been created more recently in Australia for group action lies in litigation funders, which provide the money to fund the litigation and at the same time bears the risks of the costs orders that follow from adverse judgments. For the mitigation of agency costs, the litigation funders would invariably require a suitable measure of control over the course of the litigation. However, until the recent decision of the High Court of Australia in *Campbells Cash and Carry Pty Limited v Fostif Pty Limited*, it was an unresolved question whether such litigation funding arrangements outside the context of insolvency litigation ran foul of the public policy considerations that inspire the law on maintenance and champerty. According to the Australia Financial Review, there have been nine shareholder class actions since 1998; those underwritten by litigation funders were bogged down by legal challenges targeted at the funding

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arrangements. Fostif is expected to usher in more class actions against directors, and by extension class actions for securities manipulation. In Singapore, there are at present no litigation funders – which goes toward explaining the paucity of group actions.

In Singapore, the prospect of securities litigation for market manipulation is also diminished by a very important fetter found in s 234 of the Securities and Futures Act. An action under s 234 can only be maintained against a person who has obtained a gain or suffered a loss from his market misconduct; further, the claims are limited to the amount of gain obtained or the loss avoided. The benefit accruing to the defendant thus forms the ceiling on the amount that can be recovered by the investors who suffer loss from the manipulative statements or conduct. This limitation to the amount that can be claimed adds to disincentives for litigation. It is thus little surprise that no securities litigation has thus far been commenced in Singapore despite the steady trickle of market misconduct cases. While this usefully serves to limit the liability of those found to have engaged in market manipulative conduct, it also seriously diminishes the investors’ rights to compensation.

In the context of Australia, however, the Fostif decision portends more class actions, whether by shareholders against the company, or by investors against those suspected of market misconduct. The ‘controls’ will have to be found elsewhere, for example, whether the economics of funding particular actions bear out a decision to institute a suit, and the inevitable regulations that will be created to regulate such funding. In the context of litigation, further checks will also be found in the evidential difficulties of proving market manipulation and the restraints on the process of discovery.

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65 “High Court ruling triggers new wave of class actions” Australian Financial Review (31 August 2006).
66 See for example, Michael Pelly, “State seeks greater control of firms funding litigation: Judges concerned at conduct” Sydney Morning Herald (25 July 2006).
67 Federal Court Rules O. 15 r. 15 (Court not to make an order for discovery ‘unless satisfied that the order is necessary…’) Where one party but not the other has documents relating to a matter in question, a case for discovery is prima facie established; this, however, is subject to the well exception that discovery should not be ordered to enable a mere ‘fishing expedition’: Trade Practices Commission v CC (New South Wales) No. 4 (1995) ATPR 41-425, per Lindgren J. Lindgren J further explained that what this means is that “discovery must not be used for the purpose of ascertaining a case exists, as distinct from the purpose of compelling the production of documents where there is already some evidence that a case exists.” (ibid at para. 49) A plaintiff is normally required to plead facts with sufficient particularity so that the
IV. CONCLUSION

Having examined the limitations of the common law in protecting investor’s rights against market manipulation in Part II, we observed in Part III how the three jurisdictions have responded differently to its inadequacy. In market manipulative statements, Australia and Singapore have moved beyond the strictures of the common law on misrepresentation by removing - expressly in the former and implicitly in the latter – the need to prove reliance. In so doing, it not only removes a significant obstacle to investors claiming against the manipulator; at the theoretical level, the statutory action transforms the investor protected interest from one premised on one’s reliance upon fraudulent or negligent statements, to an interest in the integrity of the price formation mechanism.

In market manipulative conduct, it is of course possible to carve out certain types of conduct as presumptively manipulative. Whether this presumption be rebuttable or irrebuttable is a policy choice. What is interesting about the rebuttable presumption, at least in the context of Singapore, is that it adopts the causation logic that is the mirror image to that found in common law deceit. In fraud, it suffices that the deceit is one of the operative causes. The exculpatory provision found in Singapore allows the defendant to escape liability by showing that no manipulative intent animated the trade.

We examined the steady move toward objective tests of market manipulation which attempts to dispense with the element of intent. While the motive for this is easily understood (and may even be necessary), the present use of concepts like “false and misleading market” without more does not dispense with what I term the “irreducible relevance of motive”. At heart, manipulative conduct is very much about the motive of defendants knows the case that they have to answer: Australian Competition and Consumer Commission v Golden West Network Pty Ltd [1997] FCA 792, Spotwire Pty Ltd v Visa International Service Association (No. 2) [2004] FCA 571 (7 May 2004).

The rules of discovery in Singapore are framed in fairly broad terms. Rules of Court O. 24 r. 8. Nonetheless, Singapore courts guard against ‘fishing expeditions’ in which an applicant hopes to obtain by the process of discovery documents otherwise unnecessary and unnecessary to the issues disclosed on the face of the claim. One indication that an applicant is embarking on a ‘fishing expedition’ is where the documents sought are framed in extremely wide terms and lack specificity: Wright Norman v Overseas-Chinese Banking Corp Ltd [1992] 2 SLR 710, [1992] SGCA 49, affirming the judgment of Chao Hick Tin J [1989] SLR 580.
the trader. A trader who purchases a large bloc of shares may be motivated by his evaluation of the worth of the shares; however, if he is motivated to move the price of the shares upwards, that motive is impugned. Alternatively, he may be selling the shares arising out of his liquidity needs; however, if he is selling at the same time to reap a collateral benefit under an Over-The-Counter contract which settlement depends on the price of this security, the trade is impugnable. Such significant trades do not, in themselves, evidence market manipulative conduct; it is the motive that helps discriminate whether the trade is a legitimate or illegitimate one. Accordingly, my contention is that the prosecution /plaintiff, whose burden it is to prove a false or misleading market, need to adduce evidence of illegitimate motive if the claim is to succeed.

Insofar as Singapore and Australia have civil liability provisions that piggy-back on the regulatory provisions on market rigging and market manipulation, they are of course a welcome addition to the armory of investors’ rights. My argument relating to the irreducible relevance of motivations does not detract from investors rights. It is a device by which one grants to traders a zone of freedom for otherwise legitimate trading. Importantly, it also serves as a barrier against nuisance suits. Apart from being conceptually sound, the irreducible relevance of motives theory safeguards ‘deep-pocket’ investors against strategic litigation. This safeguard has to be strengthened by other procedural devices, for example, strict scrutiny of the pleadings so that nuisance suits can be eliminated, and secondly, strict rules on discovery so as to prevent ‘fishing expeditions.’

The U.K. has not adopted piggy-back provisions that ride on the prohibitions against market manipulation. Given the broad presumptive liability for market abuse from unusual trading under FSMA s 118(5), it would be an unsuitable formulation by which to found a right of private action. It is probably just as well that there is no right to claim compensation for breach of the statutory duty. Viewed in perspective, however, the U.K. investor will have to look to prophylactic efficacy of the regulatory system since her rights to compensation remain largely confined within the limitations of the common law.