

BSM Market Surveillance: *cases of market manipulation and insider trading*

7th IOSCO AMCC Training Seminar

Tokyo, April 2014

Visit BSM website

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Regulatory framework

Case 1 – Market manipulation

Case 2 – Artificial conditions and market manipulation

Case 3 – Artificial conditions by offers (layering)

Case 4 – Insider trading

- IOSCO Objectives and Principles of Securities Regulation
 - Principles for Secondary Markets
 - ✓ **Principle 36:** Regulation should be designed to detect and deter manipulation and other unfair trading practices.

- The Brazilian regulatory framework
 - Law 6385/1976
 - ✓ Makes provisions on the securities market and establishes the Brazilian Securities Commission (CVM)
 - ✓ Provides that exchanges are auxiliary regulatory entities responsible for surveilling market activities and market participants
 - CVM Instruction 461/2007
 - ✓ Regulates and governs regulated securities markets and makes provisions on the formation, organization, operation and extinction of stock exchanges, commodities exchanges, futures exchanges and organized over-the-counter markets

- The Brazilian regulatory framework (cont.)
 - CVM Instruction 8/1979
 - ✓ I - Managers and stockholders of public companies, intermediaries, and other participants in the securities market are prohibited from creating artificial conditions of demand, supply, or price of securities, from engaging in price manipulation, in the execution of fraudulent operations, and in the use of unfair practices.
 - ✓ II - For the purposes of this Instruction, the following concepts shall apply:
 - a) **artificial demand, supply or price conditions** of securities are those created as a result of trades performed by participants or intermediaries that, due to fraudulent action or intentional omission, cause direct or indirect alterations in the flow of purchase or sale orders for securities;
 - b) **price manipulation** on the securities market is the utilization of any process or stratagem intended directly or indirectly to raise, maintain, or lower the quotation of any security, inducing third parties to purchase and sell it;
 - c) **fraudulent trading** on the securities market is that which uses deceptions or stratagems to induce or maintain third parties to commit errors, for the purposes of obtaining illicit equity gains for the parties involved in the operation, the intermediaries or third parties;
 - d) **unfair practice** on the securities market is that which directly or indirectly results, effectively or potentially, in treatment for any of the parties in negotiations involving securities, which places them in an improper position of imbalance or inequality with respect to the other participants in the transaction.

- The Brazilian regulatory framework (cont.)
 - BM&FBOVESPA rules

Regulatory framework

Case 1 – Market manipulation

Case 2 – Artificial conditions and market manipulation

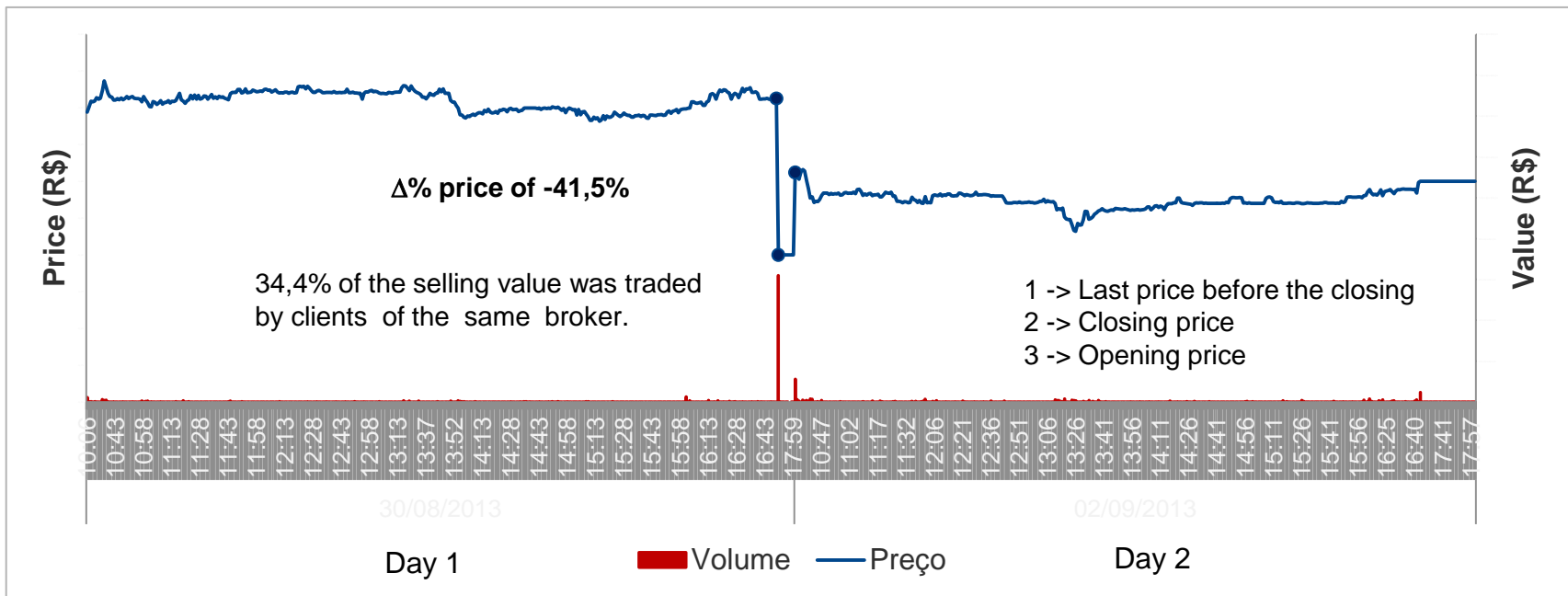
Case 3 – Artificial conditions by offers (layering)

Case 4 – Insider trading

Case 1

Market manipulation

- Manipulation by uncovered sell position at the closing to reduce the price in the day before the increase of representativeness of the stock in the Bovespa index (increase in manipulation impact on Ibovespa)
- Manipulator was long in Ibovespa futures and won with the settlement
- There was a failure to delivery in half of the uncovered sell positions
- Manipulator and beneficiary is an institution related to the broker



- **Result = + R\$ 10,6 millions = + R\$ 20,7 millions (Future) - R\$ 10,1 millions (spot)**

- BSM Action
 - Open of an Administrative Proceeding

Regulatory framework

Case 1 – Market manipulation

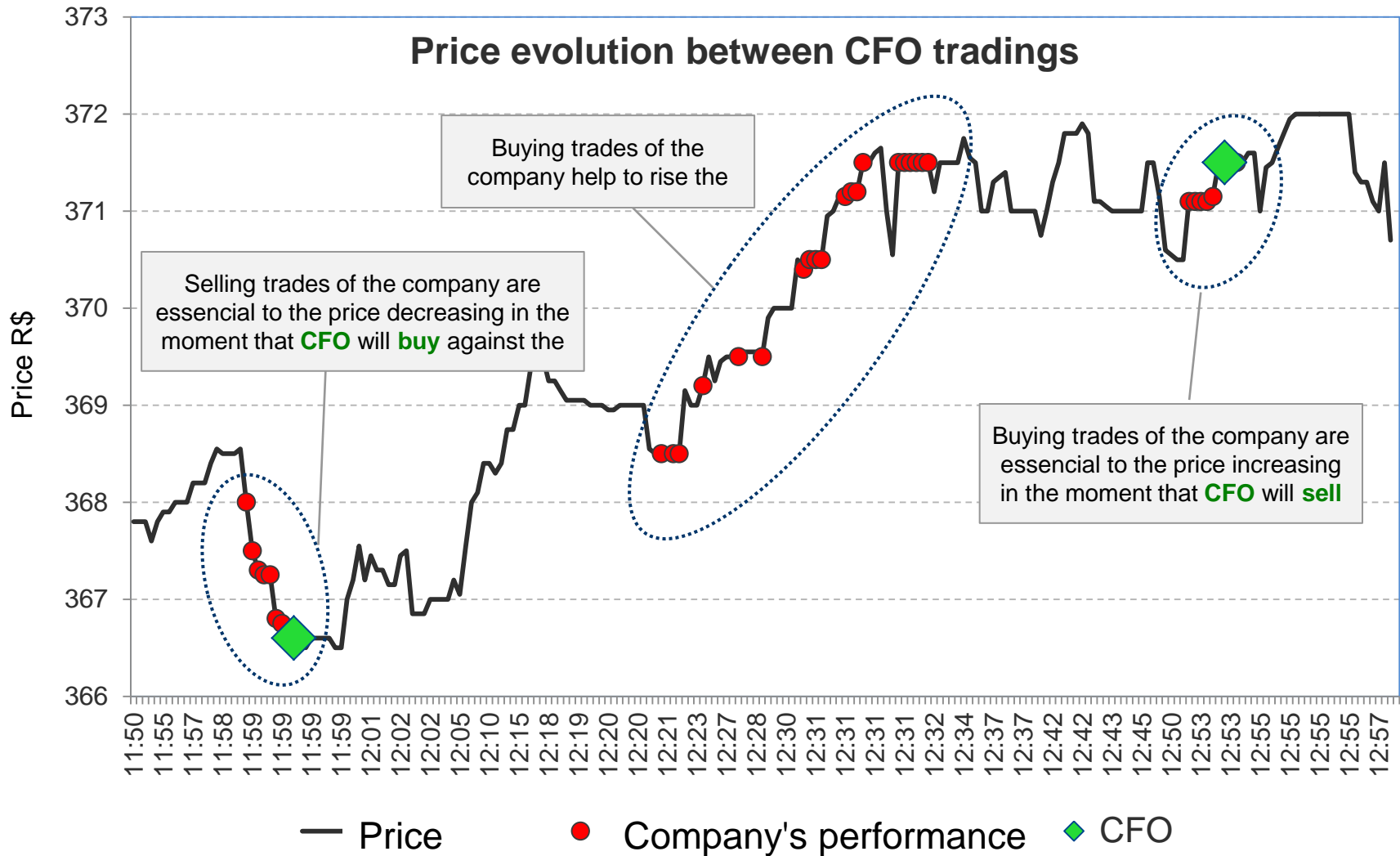
Case 2 – Artificial conditions and market manipulation

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Case 2

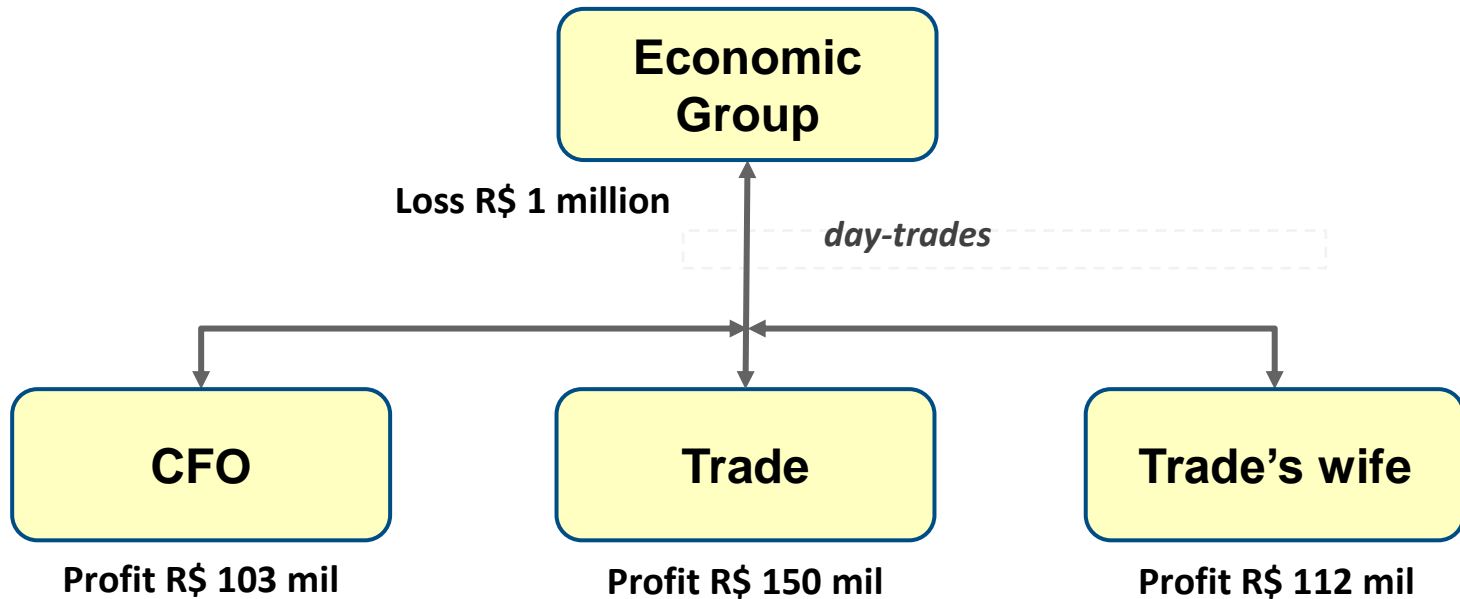
Artificial conditions and market manipulation



Case 2

Artificial conditions and market manipulation

- CFO is partner and authorized to give orders in name of the companies from the same economic group
- All trading (day trading) are executed by the same trade
- Period: 55 days during 4 months



Case 2

Artificial conditions and market manipulation

- BSM's Action
 - Administrative Proceeding initiated in 2012
 - ✓ Settlement Agreement: R\$ 1,2 millions
 - ✓ Judgement for violations related to ICVM 301

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Case 3

Artificial conditions by offers (layering)

- Manipulator raised the bid price (from 12,56 to 12,60) to sell;
- The steps created in the bid side attract buyers and the manipulator alternate to the other side of the book to sell;
- There are trading in which the manipulator is the buyer and the seller to clean the book and achieve the attracted buyer;
- After the trade, manipulator cancelled the rest of the bid offers (artificial offers).



Case 3

Artificial conditions by offers (layering)

- Manipulator repeat the strategy on the other side of the book to buy at lower price and obtain profit in day trading



- Manipulator executes the strategy in 45 days, with total of 69.600 tradings
- Total profit of the strategy: R\$106.000,00

Case 3

Artificial conditions by offers (layering)

- BSM Action
 - Accusation Term in process

Regulatory framework

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Case 2 – Artificial conditions and market manipulation

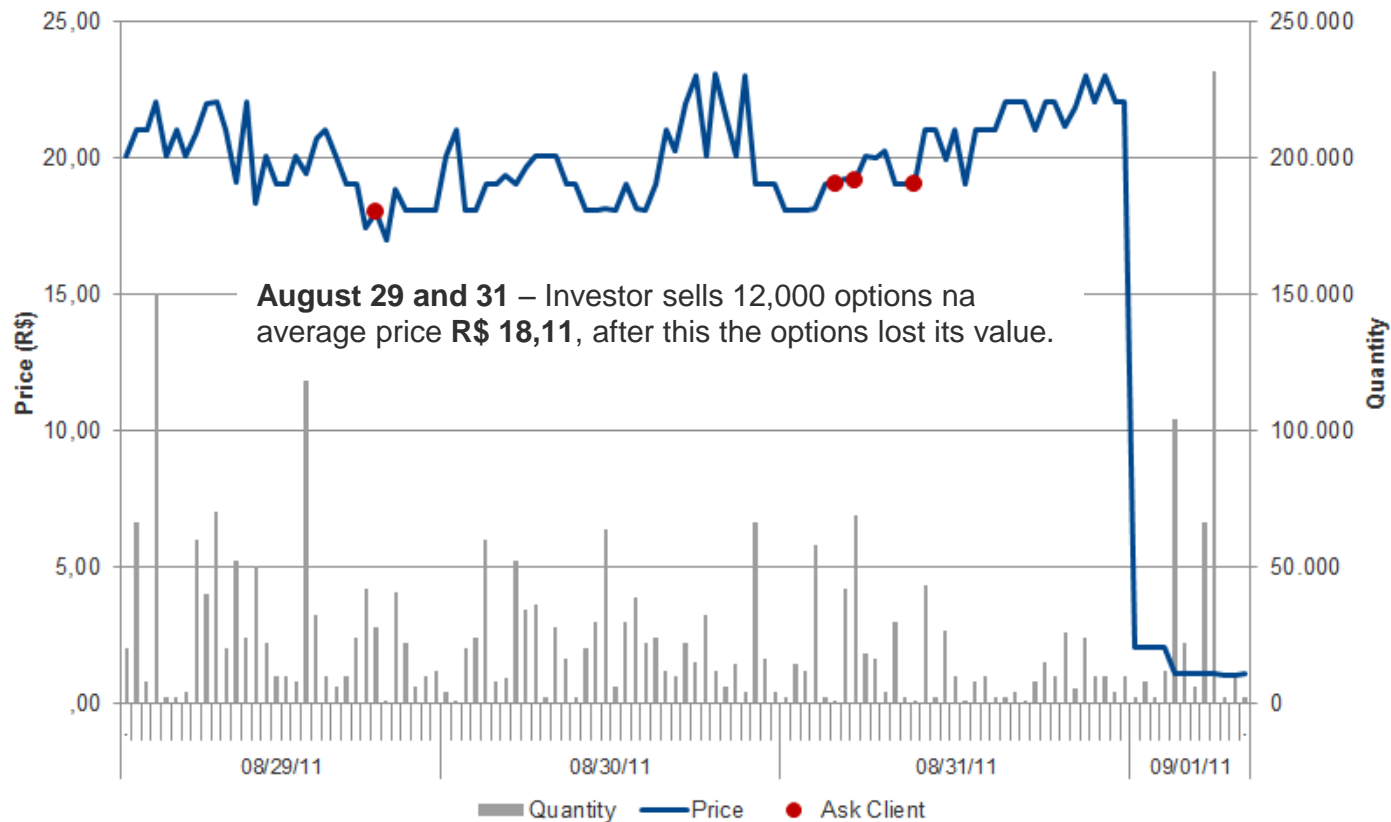
Case 3 – Artificial conditions by offers (layering)

Case 4 – Insider trading

Case 3

Insider trading

- Non expected decision from Banco Central do Brasil reducing basic interest rate (SELIC)
- Investor trading outside his pattern (sells DI options (future interest rate contract)) with profit of R\$ 217 mil



Case 3

Insider trading

- BSM's action
 - Investigation sent to CVM



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