

# Why market abuse could cost you money –

The revised Code of Market Conduct is here to help protect you

June 2008



## This factsheet is for you if:

- you deal in stocks and shares, bonds, unit trusts and investment trusts, futures and options, or 'over-the-counter' products such as spread bets in stocks.

## You need to be aware of the revised Code of Market Conduct because:

- it includes changes resulting from the Market Abuse Directive;
- it helps protect you; and
- it helps everyone know where they stand and what standards are expected of them.
- Our strategy and key objectives for tackling market abuse

## What is the Market Abuse Directive?

The Market Abuse Directive came into force on 1 July 2005. It is a law that aims to fight cross-border market abuse by establishing a common approach among EU member states. We have updated the Code of Market Conduct to include the changes resulting from this Directive – see [Where can I get more information?](#) overleaf for how to get copies of the Code.

## What is market abuse?

Seven types of behaviour can amount to market abuse – see below for more detail. The examples illustrate the abusive behaviour the Code covers.

1. Insider dealing – when an insider deals, or tries to deal, on the basis of inside information. Improper disclosure and misuse of information are kinds of insider dealing – see below.
2. Improper disclosure – where an insider improperly discloses inside information to another person.

## For example

An employee finds out that his company is about to become the target of a takeover bid. Before the information is made public, he buys shares in his company because he knows a takeover bid may be imminent. He then discloses the information to a friend.

This behaviour creates an unfair market place because the person who sold the shares to the employee might not have done so if he had known of the potential takeover. The employee's friend also has this information and could profit unfairly from it.

- Misuse of information – behaviour based on information that is not generally available but would affect an investor’s decision about the terms on which to deal.

### **For example**

An employee learns that his company may lose a significant contract with its main customer. The employee then sells his shares, based on his assessment that it is reasonably certain the contract will be lost.

This behaviour creates an unfair market place as the person buying the shares from the employee might not have done so had he been aware of the information about the potential loss of the contract.

- Manipulating transactions – trading, or placing orders to trade, that gives a false or misleading impression of the supply of, or demand for, one or more investments, raising the price of the investment to an abnormal or artificial level.

### **For example**

A person buys a large number of a particular share near the end of the day, aiming to drive the stock price higher to improve the performance of their investment. The market price is pushed to an artificial level and investors get a false impression of the price of those shares and the value of any portfolio or fund that holds the stock. This could lead to people making the wrong investment decisions.

- Manipulating devices – trading, or placing orders to trade, which employs fictitious devices or any other form of deception or contrivance.

### **For example**

Buying shares and then spreading misleading information with a view to increasing the price. This could give investors a false impression of the price of a share and lead them to make the wrong investment decisions.

- Dissemination – giving out information that conveys a false or misleading impression about an investment or the issuer of an investment where the person doing this knows the information to be false or misleading.

### **For example**

A person uses an internet bulletin board or chat room to post information about the takeover of a company. The person knows the information to be false or misleading. This could artificially raise or reduce the price of a share and lead to people making the wrong investment decisions.

- Distortion and misleading behaviour – behaviour that gives a false or misleading impression of either the supply of, or demand for, an investment; or behaviour that otherwise distorts the market in an investment.

### **For example**

The movement of an empty cargo ship that is used to transport a particular commodity. This could create a false impression of changes in the supply of, or demand for, that commodity or the related futures contract. It could also artificially change the price of that commodity or the futures contract, and lead to people making the wrong investment decisions.

## What is an 'insider'?

An 'insider' is any person who has inside information:

- as a result of their membership of the administrative, management or supervisory body of an issuer of qualifying investments;
- as a result of holding capital of an issuer of prescribed investments;
- as a result of having access to the information through their employment, profession or duties;
- as a result of criminal activities; or
- which they have obtained by other means, eg a tip-off from a friend, and which they know, or could be reasonably expected to know, is inside information.

## What is 'inside information'?

This is precise information that is not generally available and that a reasonable investor would use to help them make investment decisions. It is also information that, if generally available, would be likely to significantly affect the price of an investment.

Information from research or analysis is deemed to be generally available, and is not inside information. For example, if a passenger on a train passing a burning factory calls their broker and instructs them to sell shares in the company that owns the factory, the passenger would be acting on information that is generally available. This is because they obtained it legitimately by observing a public event.

## What is a 'regular user'?

The Code of Market Conduct states that, in some cases, behaviour will be market abuse where it falls below the standards expected by the 'regular user'. A regular user is effectively a reasonable person who deals regularly and understands the workings of the market concerned. In some places, the Code employs a 'reasonable person' test similar to the one that has often been used in the English courts.

## How does this work in relation to the criminal regime?

The Code will continue to work alongside criminal law but will apply to a wider range of activities. The existing criminal offences of insider dealing and market manipulation will remain and continue to carry very stiff penalties against someone found guilty – up to seven years in jail. Market abuse as defined in the Code is not a criminal offence, so conviction will not result in a jail sentence. However, we can seek to impose an unlimited fine if we can prove that market abuse has occurred.

## Who is affected?

The Code affects everyone who participates in, or whose conduct affects, the UK's financial markets. It makes no difference whether or not the person is regulated by the FSA, or based in the UK or overseas, or whether they are professional or retail investors. The Code also covers behaviour that takes place in the UK in relation to investments traded on other European regulated markets.

## What investments and markets are covered by the Code?

The Code applies to behaviour that occurs in relation to all investments traded on the UK's 'prescribed markets', as well as those traded on other European regulated markets.

The prescribed markets in the UK are:

- EDX London Ltd;
- London Stock Exchange Plc (including AIM);
- virt-x;
- International Petroleum Exchange;
- LIFFE;
- London Metal Exchange;
- OFEX.

Please remember that the Code covers trading of these investments and related products that is carried out both via exchanges and 'over-the-counter'.

**For example**, a person may have relevant, unpublished information about a particular company's shares. They could then choose to take advantage of this information by using a spread bet based on the price of the company's shares rather than investing in the shares themselves. But by doing this they could still be found to have committed market abuse.

## What should I do if I become aware of potential market abuse?

If you become aware of potential market abuse, we'd like to hear about it. Please contact us on this special email address or telephone number:

e-mail: [market.abuse@fsa.gov.uk](mailto:market.abuse@fsa.gov.uk)

Helpline: 0207 066 4900

## Where can I get more information?

For more information about our work on market abuse see our market abuse pages on the Fighting Financial Crime pages of our website at [www.fsa.gov.uk](http://www.fsa.gov.uk). You can download copies of the Code of Market Conduct from the FSA website at [www.fsa.gov.uk](http://www.fsa.gov.uk) or order copies from the FSA Publications Line on 0845 608 2372 at a cost of £95 each.

**If, after reading this factsheet, you have any general queries, our Market Abuse helpline will try to clarify things for you.**

**We produce a range of guides for consumers on money matters which are available from our website at [www.moneymadeclear.fsa.gov.uk](http://www.moneymadeclear.fsa.gov.uk) or can be ordered from the Consumer helpline on 0845 606 1234 (call rates may vary).**