Securities Services Act 36 of 2004 (Part 1)

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> 'An integrated and efficient financial market requires market integrity. The smooth functioning of securities markets and public confidence in markets are prerequisites for economic growth and wealth. Market abuse harms the integrity of financial markets and public confidence in securities and derivatives.'**

1 Introduction

It is disturbing to observe that South African financial markets have weakened considerably in recent years, posing a danger to the local African economy.[1] One reason for this state of affairs is that international banks and other speculators with unlimited financial resources have been engaging in market manipulation.[2] Market manipulation generally involves an attempt to interfere with the operation of the market.[3] Most stock markets operate on the principle of a free market, according to which supply and demand regulate the price of securities so that, presumably, the price of a security reflects its true value.[4] Any interference with this process of price determination amounts to market manipulation.[5] Market manipulation may result in investors being misled into buying worthless shares or selling their otherwise valuable investments at a loss.[6]

The Securities Services Act 36 of 2004 (the 'SSA'),[7] which came into effect on 1 February 2005, has as two of its declared objects the promotion of the international competitiveness of securities services[8] in South Africa and the

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** Recital 2 to Directive 2003/6/EC of the European Parliament and of the Council of 28 Jan 2003 on insider dealing and market manipulation (market abuse): *Official J* L96 of 12 Apr 2003 (the 'EU Market Abuse Directive').

[1] See the *Memorandum on the Objects of the Companies Amendment Bill*, 1999, B 17D-99.

[2] Ibid.

[3] See the New Zealand Ministry of Economic Development *Reform of Securities Trading Law: Volume Two: Market Manipulation Law Discussion Document* (2002) in par 41, available at *http://www.med.govt.nz/templates/MultipageDocumentPage____6861.aspx* (last consulted on 17 Mar 2008).

[4] See JJ Henning & S du Toit 'High-pressure Selling of Securities: From Rigging the Market to False Trading, Market Manipulation and Insider Dealing' (2000) 21 *The Company Lawyer* 257 at 257.

[5] Ibid.

[6] See Shazeeda Ali 'Market Abuse: It's not Just a Wall Street Thing' (2006) 27 *The Company Lawyer* 222 at 222.

[7] The SSA repealed and replaced the Stock Exchanges Control Act 1 of 1985, the Financial Markets Control Act 55 of 1989, the Custody and Administration of Securities Act 85 of 1992, and the Insider Trading Act 135 of 1998 and consolidated them into one piece of legislation.

[8] Section 2(*d*) of the SSA. Section 1 defines 'securities services' as services provided in terms of the SSA in respect of (*a*) the buying and selling of securities; (*b*) the custody and administration of

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enhancement of confidence in the South African financial markets.[9] The SSA aims to achieve these objects firstly by requiring securities services to be provided in a fair, efficient and transparent manner, and secondly by contributing to the maintenance of a stable financial market environment.[10] In accordance with this aim, detailed legislative provisions have been enacted in the SSA to regulate the offence of market abuse, which is contained in Chapter VIII of the SSA. 'Market abuse' is described in the SSA as constituting three offences: insider trading; engaging in a prohibited trading practice; and the making or publishing of false, misleading or deceptive statements, promises and forecasts. This article will discuss and analyse only the latter two offences,[11] which together constitute market manipulation, and which will be collectively referred to as such.

Although market manipulation has become increasingly important in recent years and although more international focus has been placed on eliminating and regulating it, it is not by any means a novel concept. The American Securities and Exchange Commission was established at the beginning of the last century in response to a stock market which was plagued by insider trading and market manipulation.[12] In South African law, market manipulation is prohibited by our common law and was statutorily prohibited in the now repealed Stock Exchanges Control Act of 1985 and the Financial Markets Control Act of 1989.[13] As at 13 April 2007, the JSE Securities Exchange had since the enactment of the SSA referred about seven cases of market manipulation to the Financial Services Board (the 'FSB').[14] It was recently reported that the FSB had launched a full forensic investigation into market manipulation stemming from a story published on 11 April 2007 by financial news agency Bloomberg News that a consortium led by an unknown American financier had made a bid of USD12.5 billion for mining house Gold Fields Limited, which resulted in Gold Fields' shares increasing by 11 per cent on 11 April 2007 and adding almost R10 billion to the market value of its shares.[15] The prevailing view was that the story was a hoax.[16]

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securities; (*c*) the management of securities by an authorised user; (*d*) the clearing of transactions in listed securities; and (*e*) the settlement of transactions in listed securities.

[9] Section 2(*a*) of the SSA.

[10] Section 2(a)(*i*) and (*ii*) of the SSA.

[11] For a critical discussion on the insider trading provisions of the SSA, see Rehana Cassim 'Some Aspects of Insider Trading – Has the Securities Services Act 36 of 2004 Gone Too Far?' (2007) 19 *SA Merc LJ* 44.

[12] *Central Bank of Denver NA v First Interstate Bank of Denver NA* 511 US 164 (US SC,1994) at 170-1; *Ernst & Ernst v Hochfelder* 425 US 185 (US SC,1976) at 194; Ali op cit note 6 at 222.

[13] The Stock Exchanges Control Act in s 1 prohibited the manipulation of 'securities', which included stocks, shares and debentures, while the Financial Markets Control Act of 1989 in s 1 prohibited the manipulation of 'financial instruments', which included futures contracts, option contracts and loan stock on a financial market.

[14] See the report by Justin Brown 'FSB May Probe Bloomberg Story on Gold Fields' 13 Apr 2007 *Business Report* at 1.

[15] See Justin Brown 'Gold Fields Zooms 11% on Bid Talk' 12 Apr 2007 *Business Report* at 1.

[16] When questions were raised as to whether the offer was realistic, the price of Gold Fields' shares dropped. This movement in the share price prompted the FSB to launch an investigation into whether there had been any market manipulation. Key issues behind the investigation were whether Bloomberg News had been negligent in publishing information which it knew was false or ought to have known

There are two ways in which to examine the harm that may be caused by manipulative conduct. Firstly, it is regarded as being a wrong against those individuals directly affected, such as those who trade on the basis of false information about the price or trading volume caused by the market manipulation.[17] This approach leads to market manipulation being regarded as a form of fraud.[18] Secondly, it may be regarded as a wrong against the market, in the sense that it undermines public confidence in the markets as investors lose confidence in its integrity.[19] This article will examine which of these two approaches has been adopted in the SSA.

The regulation of market manipulation in South Africa is relatively new and our jurisprudence on market manipulation is still very much in its early stages of development. It is therefore useful to examine how market manipulation is regulated in other jurisdictions. As one of the objects of the SSA is to promote the international competitiveness of securities services in South Africa, it is important that the provisions of the SSA regulating market manipulation are in harmony with the equivalent international legislation. Compliance with international standards would appeal to both local investors as well as foreign investors, who would then have the assurance that this country does have adequate protection for market security.[20] This article will examine whether, and to what extent, the legislation regulating market manipulation in the SSA is in harmony with that in other leading foreign jurisdictions, namely America, the European Union, the United Kingdom, and Australia. It will become evident from the discussion of market manipulation in these jurisdictions that the SSA has borrowed extensively, sometimes even in exact terms, from these jurisdictions. Accordingly, judicial interpretation of the legislation regulating market manipulation in these jurisdictions will be an invaluable guide to the interpretation of the market manipulation provisions of the SSA.

The SSA does not define 'market manipulation' but describes instead practices that are to be regarded as manipulative of the market. Section 75(1) of the SSA prohibits trade-based market manipulation, which involves techniques designed to distort the market and entails conduct that interferes with the normal market mechanisms of supply and demand for a security.[21] Section 75(3) of the SSA goes so far as to deem certain trading practices to be manipulative, while s 76 prohibits disclosure-based market manipulation.

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was false, and whether those responsible for the release of the information had profited by trading in Gold Fields' shares before and after the information had been published. The FSB sought assistance for its investigation from the American Securities and Exchange Commission. See the reports by Ronnie Morris 'Media May Feel Regulator's Wrath over Gold Fields "hoax bid" ' 13 Apr 2007 *Business Report* at 2; Charlotte Mathews 'FSB Takes Close Look at Gold Fields "offer" ' 13 Apr 2007 *Business Day* at 1; Julie Bain 'Questionable Bid Takes Shine off Gold Fields' 15 Apr 2007 *Sunday Times Business Times* at 5; Justin Brown 'FSB wants SEC to Help Probe Pastorini Saga' 16 Apr 2007 *Business Report* at 1.

[17] See the NZ Ministry of Economic Development op cit note 3 in par 44.

[18] Ibid.

[19] Ibid.

[20] Idem in par 32.

[21] Idem in par 64; Ali op cit note 6 at 222.

This entails the dissemination of inaccurate information relating to the demand, supply, price or value of a security.[22]

This article is divided into three sections. In the first, the regulation of market manipulation at common law will be canvassed and the trading practices prohibited by s 75(1) of the SSA will be examined. Then I will examine the trading practices which s 75(3) of the SSA deems to be manipulative as well as the disclosure-based market manipulation provisions of s 76 of the SSA. Finally, I will examine the defences to market manipulation as provided for by the SSA and the penalties stipulated for the offence. I will conclude that the provisions of the SSA regulating market manipulation are commendably internationally competitive and are for the most part in harmony with foreign legislation, and, in certain instances, even more far-reaching than legislation elsewhere. But a potential weakness of South Africa's market manipulation regime, compared with foreign legislation, is the paucity of defences to market manipulation in the SSA, which could easily discourage legitimate trading. A further more serious weakness is the absence of a statutory civil remedy for market manipulation, which could have the effect of not effectively deterring persons from engaging in market manipulation and of denying victims of market manipulation the opportunity to recover their losses.

2 The Rationale of Regulating Market Manipulation

The objective of manipulating the market is to make money, either directly through transactions or by other means.[23] For instance, in the recent Gold Fields saga it was said that if a Gold Fields executive had bought 100 000 of its shares at the closing price of R137.50 on the day before the story concerning it was published, and had sold these shares at the intraday high of R152.50 to which the shares rose to on the publication of the story, the executive would have made a gross profit of R1.5 million.[24]

Those in a position to manipulate the market include issuers of securities, participants in the securities market, market intermediaries, and a combination of these persons acting in co-operation or in concert with each other.[25] A number of factors cause a person to manipulate the market. For example, a market manipulator would attempt to influence the price of a security so that he could buy the securities at a lower price, combat competitive transactions, or influence take-over bids or other large transactions.[26] In a hostile take-over,

[22] Ibid.

[23] See the Technical Committee of the International Organization of Securities Commissions Public Document No 103 *Investigating and Prosecuting Market Manipulation* (May 2000), available at *http://www.iosco.org/library/pubdocs/pdf/IOSCOPD103.pdf* (last visited on 17 Mar 2008) at 6.

[24] See Quentin Wray in 'Gold Fields Has a Lot to Answer for on Pastorini Bid Lead' 18 Apr 2007 *Business Report* at 18.

[25] See the Technical Committee of the International Organization of Securities Commissions op cit note 23 at 7.

[26] Idem at 6.

the directors of the target company would have an interest in seeing that the price of the securities of the target company on the market is higher than the bid price, in order to reduce the likelihood that shareholders in the target company would vote in favour of the bid, while at the same time the bidder would have an interest in seeing the price of those securities declining on the market.[27] Even in the absence of a take-over offer, the management of a public company would be concerned that if the price of the company's shares were to fall, the company would be vulnerable to a take-over bid.[28]

In the American decision in *The Trane Company v O'Connor Securities*,[29] the Court stated that the main purpose of the legislative prohibition of market manipulation was 'not to prohibit market transactions which may raise or lower the price of securities, but to keep an open and free market where the natural forces of supply and demand determine a security's price'.[30] In *United States v Brown*,[31] the Court articulated the concept of a free market as follows:

> 'When an outsider, a member of the public, reads the price quotations of a stock listed on an exchange, he is justified in supposing that the quoted price is an appraisal of the value of that stock due to a series of actual sales between various persons dealing at arm's length in a free and open market on the exchange, and so represents a true chancering of the market value of that stock thereon under the process of attrition due to supply operating against demand.'[32]

Regulation of market manipulation was formalised in America in the 1930s when Congress was persuaded that there was a link between the manipulation of security prices that had caused the excessive speculation resulting in the stock-market crash of 1929 and the depression of the 1930s.[33] Two statutes primarily regulate market manipulation in America: the Securities Exchange Act of 1933[34] and the Securities Exchange Act of 1934.[35] At the time of the introduction of the Bill that became the Act of 1934, the Chairman of the Senate Committee on Banking and Currency stated the following in relation to the general purpose of the legislation:

> 'Manipulators who have in the past had a comparatively free hand to befuddle and fool the public and to extract from the public millions of dollars through stock-exchange operations are to be curbed and deprived of the opportunity to grow fat on the savings of the average man and woman of America. Under this bill the securities exchanges will not only have the appearance of an open market place for investors but will be truly open to them, free from the hectic operations and dangerous practices which in the past have enabled a handful of men to operate with stacked cards against the general body of the outside investors.'[36]

In the same vein the Australian High Court stated in *North v Marra*

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[27] See Ashley Black 'Regulating Market Manipulation: Sections 997-999 of the Corporations Law' (1996) 70 *Australian LJ* 987 at 988.
[28] Ibid.
[29] 561 F Supp 301 (SD NY, 1983).
[30] At 304.
[31] 5 F Supp 81 (SD NY, 1933).
[32] At 85.
[33] See *Central Bank of Denver v First Interstate Bank of Denver* supra note 12 at 170-1; *Ernst & Ernst v Hochfelder* supra note 12 at 194.
[34] 48 Stat 74 (1933), codified at 15 USC §77*a* et seq.
[35] 48 Stat 881 (1934), codified at 15 USC §78*a* et seq.
[36] Senator Fletcher, Chairman of the Senate Committee on Banking and Currency, quoted in *Blue Chip Stamps v Manor Drug Stores* 421 US 723 (US SC,1975) at 765.

Developments Ltd[37]that the purpose of regulating false trading and market rigging was to ensure that the market reflects the forces of genuine supply and demand. By 'genuine supply and demand' the Court excluded 'buyers and sellers whose transactions are undertaken for the sole or primary purpose of setting or maintaining the market price'.[38]

Due to concerns that the European financial markets had become distorted, the European Parliament and the Council of the European Union recently adopted a Directive on insider dealing and market manipulation.[39] Some reasons for the distortion of the European financial markets were thought to be that the number of new participants that had entered the financial markets had increased, cross-border trading had increased, new products and technologies had been developed over the years, and Member States had developed diverse approaches to combat market manipulation.[40] The EU Market Abuse Directive aims to introduce a common legal framework in Europe to prevent, detect, investigate and sanction market manipulation (and insider trading), and to promote greater investor confidence in the integrity of the financial markets.[41] It requires each Member State to designate a single administrative competent authority to ensure that the provisions adopted pursuant to the Directive are applied.[42]

The United Kingdom has recently amended its legislation regulating market manipulation in order to harmonise it with the EU Market Abuse Directive.[43] In compliance with art 11 of the Directive, the Financial Services Authority has been designated as the single administrative regulator to ensure

[37] (1981) 148 CLR 42 (HC Aus).

[38] At 59.

[39] The EU Market Abuse Directive repealed and replaced the Insider Dealing Directive No 89/592/EEC (*Official J* L334 of 18 Nov 1989), which applied only to insider dealing and not to market manipulation: see art 20 of the EU Market Abuse Directive.

[40] See the Joint HM Treasury and Financial Services Authority Consultation Paper *UK Implementation of the EU Market Abuse Directive (Directive 2003/6/EC)* (18 Jun 2004), available at *http://www.fsa.gov.uk/pubs/other/eu_mad.pdf* (last consulted on 17 Mar 2008) at 5.

[41] See Recitals 11 and 12 to the EU Market Abuse Directive and the Joint HM Treasury and Financial Services Authority Consultation Paper op cit note 40 at 5.

[42] Article 11 of the EU Market Abuse Directive. All the Member States of the European Union were required to have implemented the EU Market Abuse Directive by 12 Oct 2004: see art 18 of the EU Market Abuse Directive. Only one Member State implemented the Directive on the due date. It was implemented in the UK on 1 Jul 2005: see Al-Harith Sinclair, Martin Webster & Jeremy Phillips 'Market Abuse Directive – UK Implementation on 1 July 2005' (Jul 2005), available at *http://www.pinsentmasons.com/media/1300625559.pdf* (last consulted on 17 Mar 2008).

[43] In the UK market manipulation is regulated by s 118, contained in part VIII, of the Financial Services and Markets Act, 2000 (c 8) which has now been amended by sched 2 to The Financial Services and Markets Act, 2000 (Market Abuse) Regulations, 2005 (SI 2005/381). The UK regime on market manipulation has not been made to accommodate the requirements of the EU Market Abuse Directive but the regime of the Directive has simply been superimposed on the UK regime thereby creating two market-abuse regimes. Following criticism that the UK would face two overlapping regimes, provision was made in the Financial Services and Markets Act for certain aspects of the UK regime automatically to disappear on 30 Jun 2008 by virtue of a sunset clause contained in s 118(9): see Chris Ashworth, James Perry, Glynn Bawick & David Toube 'New Market Abuse Provisions under FSMA' (May 2005), available at *http://www.ashurst.com/doc.aspx?id_Content=1815* (last consulted on 17 Mar 2008).

that the provisions adopted pursuant to the Directive are put into effect and complied with.[44]

The rationale, then, of regulating market manipulation is to maintain an open and free market where the natural forces of supply and demand determine a security's price, to achieve greater investor confidence in the integrity of the financial markets, and to protect investors from market manipulation. If investors have confidence in the fairness of the markets, the liquidity and the efficiency of the markets would be enhanced.[45] Inevitably, if investors are wary of the markets because of alleged suspect market practices, they would be inclined to move their cash into investments that are considered to be safe and sound, or to invest in markets in other countries that are regarded as being credible.[46] In Australia, where market manipulation is prohibited by the Australian Corporations Act, 2001,[47] the Australian High Court went so far in *North v Marra Developments Ltd*[48] as to assert that it is in the interests of the community as a whole that the security market is free from manipulation.

Most critics of market-manipulation practices hold the view that such practices ought to be statutorily prohibited and regulated. But not all critics are of this view. One reason propounded for not statutorily regulating market manipulation is that excessive regulation of market behaviour inhibits legitimate market activity.[49] A compounding fear is that if the legislation that prohibits market manipulation is drafted too widely, it could prohibit conduct which may otherwise be efficient.[50] It is submitted that these fears are well grounded and that over-regulation of market manipulation must be guarded against so as not inadvertently to inhibit legitimate and efficient market activity.

Two critics that are strongly of the view that market manipulation ought not to be statutorily prohibited are Fischel and Ross, who contend that trade-based market manipulation should not be legislatively prohibited because it is inherently self-deterring as the chances of it being profitable are quite low.[51] They assert that in order for market manipulation to be profitable, two conditions must be met: the trading must cause the price of the relevant security to rise, and the manipulator must be able to sell the security at a price that is higher than that at which he or she purchased the security, inclusive of the transaction costs.[52] They contend that it is very difficult to satisfy both conditions simultaneously as purchases seldom move prices up and if they do,

[44] Joint HM Treasury and Financial Services Authority Consultation Paper op cit note 40 at 12.

[45] Technical Committee of the International Organization of Securities Commissions op cit note 23 at 2.

[46] Ali op cit note 6 at 224.

[47] Act 50 of 2001, in ch 7, part 7.10, division 2.

[48] Supra note 37 at 59.

[49] See Ali op cit note 6 at 224.

[50] See NZ Ministry of Economic Development op cit note 3 in par 63.

[51] Daniel R Fischel & David J Ross 'Should the Law Prohibit "Manipulation" in Financial Markets?' (1991) 105 *Harvard LR* 503 at 512-3 and 553.

[52] Idem at 512.

it is not easy to affect sales at the inflated price.[53] Regarding disclosure-based market manipulation, they contend that this is a form of fraud and cannot be considered as falling fully within the scope of market manipulation.[54] They argue further that as trading is costly, it is unlikely that attempts to manipulate security prices would be made.[55] Fischel and Ross also assert that a further reason not to legislatively prohibit market manipulation is that the enforcement of the prohibition would result in significant social costs that would outweigh the benefits.[56]

Despite these arguments against the legislative regulation of market manipulation, the fact remains that market manipulation is prevalent in financial markets and it is statutorily prohibited both in South Africa and in foreign jurisdictions.

3 The Regulation of Market Manipulation at Common Law

Market manipulation is prohibited in South Africa by the common law, where it is known as the crime of 'rigging the market'. The common-law crime of rigging the market is predominantly based on English law.[57] A 'rig' is essentially a fictitious operation.[58]

In the English decision in *Rubery v Grant*,[59] Sir R Malins VC strongly condemned the crime of rigging the market by proclaiming that

> '"[r]igging the market" . . . is one of the most dishonest practices to which men can possibly resort. There is a class of people who think it is a legitimate mode of making money; but if they would only examine it for a moment they would see that a more abominable fraud, and one more difficult of detection, cannot be found.'

In the very first English case of a market rig, *R v De Berenger*,[60] De Berenger and seven others had spread false rumours that Napoleon Bonaparte had been killed, with the object of inducing the English public in believing that the war would soon be ended. This was done in order to cause an increase in the price of British Government funds and other securities. The rig had the effect of causing prejudice to persons who had bought funds and securities on that day. The King's Bench was unanimous in holding the defendants guilty of a conspiracy to defraud. The offence in this case concerned the spreading of false rumours, but in *Scott v Brown, Doering, McNab & Co, Slaughter & May v Brown, Doering, McNab & Co*,[61] the Court remarked that there was no real

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[53] Idem at 513. In a detailed response to Fischel and Ross, Steve Thel '$850,000 in Six Minutes – The Mechanics of Securities Manipulation' (1994) 79 *Cornell LR* 219 disputes their argument that market manipulation is self-deterring.
[54] See Fischel & Ross op cit note 51 at 510-2.
[55] Idem at 512-9.
[56] Idem at 522-3.
[57] See Henning & Du Toit op cit note 4 at 257.
[58] See *R v McLachlan & Bernstein* 1929 WLD 149 at 155.
[59] (1872) 13 LR Eq 443 at 447-8.
[60] (1814) 3 M & S 67, 105 ER 536.
[61] [1892] 2 QB 724 (CA) at 730-1.

distinction between the spreading of false rumours and engaging in false and fictitious acts in order to induce the public to take shares.

In the earliest reported South African decision on rigging the market, *R v McLachlan & Bernstein*,[62] De Waal JP laid down the essential elements that are required to constitute the crime of rigging the market:

(*a*) the rigger must hold shares (generally a large parcel of shares) which he wishes to off-load to the ignorant public, and which he cannot off-load other than by the creation of a fictitious market for those shares;

(*b*) the shares must be practically valueless, or have a value which is far below that at which the rigger wishes to off-load them; and

(*c*) as a result of a successful rig, the unsuspecting public must be left with worthless shares, at which stage the rigger withdraws his support by ceasing to operate, and the shares inevitably recede to the value at which they stood before the rig had commenced.

In *S v Marks*,[63] Hill J ruled, with reference to the second and third of these requirements, that it was not a necessary element of rigging the market that the shares should be valueless or that members of the public should be left with worthless shares. The Court further modified the first requirement by stating that it is not a pre-requisite for the perpetration of a rig that the rigger must hold a parcel of shares which he wishes to off-load onto the public: it is only at the time when the rigger wishes to benefit from the result of his rigging operations that he must have had a parcel of shares to off-load at a profit on the buying public.[64] For instance, the rigger may manipulate market dealings by placing buying and selling orders without becoming the holder of any shares but with the aim of acquiring, at some stage during the rigging operation, a quantity of shares for off-loading upon the public at a later stage when the prices have risen to the desired level.[65] Alternatively, the rigger may acquire an option to buy shares, which he would then exercise at a time when he is able to make a profit as a result of his manipulation.[66]

At common law a contract which involves an attempt to deceive other traders in the market is void for illegality, even where the transaction involved an actual sale or purchase of securities.[67] In *Scott v Brown, Doering, McNab & Co, Slaughter & May v Brown, Doering, McNab & Co*,[68] the plaintiff had instructed stockbrokers to buy shares on the market at a premium to the issue price. He had done so with the sole object of inducing the public into believing that there was a bona fide market for the shares and that the shares were trading at a genuine premium. An action instituted by the plaintiff under

[62] Supra note 58 at 156.
[63] 1965 (3) SA 834 (W) at 846.
[64] At 846-7.
[65] At 847.
[66] Ibid.
[67] See Black op cit note 27 at 989.
[68] Supra note 61.

its contract with the stockbrokers failed on the ground that the contract was void for illegality. On appeal, the Court, in ruling that the contract was illegal, stated that

> '[t]he plaintiff's purchase was an actual purchase, not a sham purchase; that is true, but it is also true that the sole object of the purchase was to cheat and mislead the public . . . his illegal contract confers no rights on him'.[69]

Significantly, the statutory prohibition of market manipulation applies only to listed securities[70] whereas the common-law offence of rigging the market applies to both listed, as well as to unlisted securities. It is important to observe that the SSA does not repeal the common-law crime of rigging the market. Consequently, if an act falls outside the scope of the statutory prohibition of market manipulation in the SSA, the common-law crime of rigging the market (or other common-law remedies) could well still apply.

It has repeatedly been emphasised by the courts that it is difficult to prove the crime of rigging the market due to the complexity of the manipulative manoeuvres, which the rigger generally secretly executes and skillfully disguises.[71] The schemes are often so well planned that it is difficult to distinguish real market fluctuations from artificial price inflations.[72] Fluctuations in market prices could be due to a number of causes. In *R v McLachlan & Bernstein*,[73] the Court suggested that some of these causes may arise from the political situation, an impending general election, a general scarcity or tightness of money, or the current bank rate or rate of exchange. It is hoped that the statutory prohibition of market manipulation in the SSA, to be examined now, would make it easier to prove the offence.

4 Market Manipulation in the SSA

4.1 Prohibited Trading Practices

Section 75(1) of the SSA prohibits trade based market manipulation practices as follows:

> '**Prohibited trading practices**
> 75 (1) No person may –
> (*a*) either for such person's own account or on behalf of another person, directly or indirectly use or knowingly participate in the use of any manipulative, improper, false or deceptive practice of trading in a security listed on a regulated market, which practice creates or might create –
> (*i*) a false or deceptive appearance of the trading activity in connection with; or
> (*ii*) an artificial price for,
> that security;

[69] At 729. This general principle was approved by the High Court of Australia in *North v Marra Developments Ltd* supra note 37 at 60.

[70] The provisions in the SSA which prohibit market manipulation apply to securities listed on a regulated market. A 'regulated market' is defined in s 72 of the SSA as meaning 'any market, whether domestic or foreign, which is regulated in terms of the laws of the country in which the market conducts business as a market for dealing in securities listed on that market.' This is discussed further below.

[71] See *S v Marks* supra note 63 at 848.

[72] See Henning & Du Toit op cit note 4 at 258.

[73] Supra note 58 at 156.

(*b*) place an order to buy or sell listed securities which, to his or her knowledge will, if executed, have the effect contemplated in paragraph (*a*).'

According to s 75(1)(*a*) of the SSA, two types of trading practices are prohibited: the creation of a false or deceptive appearance of the trading activity in connection with a security listed on a regulated market, and the creation of an artificial price for such a security. Section 75(1)(*b*) of the SSA prohibits the placing of an order to buy or sell listed securities which, if executed, would again create a false or deceptive appearance of the trading activity in connection with that security or an artificial price for that security. These trading practices are discussed in more detail below.

4.1.1 'Manipulative, improper, false or deceptive practice'

In order to fall within the purview of s 75(1)(*a*) of the SSA, the trading practice in question must be one that is 'manipulative, improper, false or deceptive'. The SSA sheds no light on the meaning of these terms. The term 'manipulative' was defined as follows by the American Supreme Court in *Ernst & Ernst v Hochfelder*:[74]

> 'Use of the word "manipulative" is especially significant. It is and was virtually a term of art when used in connection with securities markets. It connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities.'

The term 'deceptive' has been subject to extensive judicial consideration in Australian law as the word appears both in legislation regulating consumer protection and in the market-manipulation provisions of the Australian Corporations Act, 2001.[75] The word 'deceptive' has been interpreted by the Australian courts in the context of consumer protection legislation to mean 'to lead into error'.[76] As the Australian courts also apply the consumer-protection tests and reasoning to market manipulation, it is very likely that in the context of the market-manipulation provisions they would likewise interpret the word 'deceptive' as meaning 'to lead into error'.[77]

4.1.2 'Use or knowingly participate'

A person would contravene s 75(1)(*a*) of the SSA if he were to 'use or knowingly participate' in the use of a manipulative, improper, false or deceptive trading practice. The word 'knowingly' in a statutory provision usually indicates that fault in the form of intention must be present for the provision to have been contravened.[78] Notably, the word 'knowingly' does not

[74] Supra note 12 at 199.

[75] See Kerry Morrell 'Changes to the Takeovers Code and Takeovers Act and an Update on the Operations of the Panel' May 2006 *Securities Law Update*, available at *http://www.takeovers.govt.nz/speeches/km-290506.pdf* (last visited on 17 Mar 2008) at 4. For instance, s 1041H of the Australian Corporations Act, 2001 prohibits misleading or deceptive conduct by a person in relation to a financial product or financial service.

[76] See Morrell op cit note 75 at 4.

[77] Ibid.

[78] See Jonathan Burchell & John Milton *Principles of Criminal Law* 3 ed (2005; revised reprint May 2006) at 501.

qualify the 'use' of a manipulative trading practice. On a literal interpretation of s 75(1)(*a*), it appears that strict liability has been imposed for using a prohibited trading practice, that is, liability without proof of intention or negligence. Strict liability relieves the prosecution of having to prove fault and could lead to a conviction despite a reasonable doubt of guilt.[79] It also deprives the accused person of any defence that excludes fault.[80]

In a minority judgment in the Constitutional Court decision in *S v Coetzee*,[81] O'Regan J asserted that strict liability under the criminal law in South Africa is unacceptable. The learned Justice stated that, as a general rule, it is a fundamental principle of democratic societies that persons who are not at fault should not be deprived of their freedom by the State.[82] However, Kentridge J was of the view that the constitutional standard would allow some degree of strict liability. In his opinion, whether a strict liability provision would infringe the Constitution would depend on the nature of the particular statutory provision under consideration and the weight of the burden on the accused.[83]

Even if the imposition of strict liability under s 75(1)(*a*) of the SSA is found not to infringe the Constitution, the question arises whether it is appropriate for strict liability to be imposed in the light of the maxim 'actus non facit reum nisi mens sit rea' (an act is not unlawful unless mens rea is present). It is on the basis of this maxim that South African courts have been reluctant, in the absence of clear and convincing indications in the relevant statute, to interpret statutory provisions which contain no express mens rea requirement as dispensing with mens rea.[84] The presumption that the Legislature intended fault to be an element of liability is fortified by the appearance in the relevant statute of words such as 'knowingly', 'maliciously', 'corruptly' and 'fraudulently' which indicate that it was the intention that innocent infringements of the statute should not be punishable.[85]

Courts in the United Kingdom, America, Australia, New Zealand and Canada have shown a reluctance to accept that a statutory offence dispenses with the requirement of fault.[86] The Securities and Exchange Commission rule 10*b*-5,[87] the most widely used provision in the enforcement of market manipulation in America, does not contain a fault requirement either, but

[79] Idem at 550.
[80] Ibid.
[81] 1997 (3) SA 527 (CC).
[82] In par 176.
[83] In par 95. This case was decided under the provisions of the Interim Constitution of the Republic of South Africa, Act 200 of 1993. Langa J and Mahomed DP found it unnecessary to consider whether strict liability was constitutionally permissible.
[84] *S v Coetzee* supra note 81 in pars 94 and 165. See, eg, *S v Arenstein* 1967 (3) SA 366 (A) at 381D-E; *S v Oberholzer* 1971 (4) SA 602 (A) at 610H-611A, and *Amalgamated Beverage Industries Natal (Pty) Ltd v Durban City Council* 1994 (3) SA 170 (A) at 173G-174A.
[85] See Burchell & Milton op cit note 78 at 500.
[86] See *S v Coetzee* supra note 81 in pars 166-71 and the cases cited there.
[87] 17 Code of Federal Regulation ('CFR') §240.10*b*-5 ('rule 10*b*-5 of the Securities Exchange Act of 1934'). Rule 10b-5 was promulgated in 1942 to implement §10(*b*) of the Securities Exchange Act of 1934 (15 USC § 78*j*(*b*)) ('§ 10(b) of the Securities Exchange Act of 1934') which in turn prohibits the use of manipulative and deceptive devices or contrivances in the sale or purchase of securities in

American courts have nevertheless read into it a requirement that the offender must have acted scienter, which was defined in *Ernst & Ernst v Hochfelder*[88] as a 'mental state embracing intent to deceive, manipulate, or defraud.'[89] The American Supreme Court in this case stated that the terms 'manipulation' and 'deception' are the commonly understood terminology of intentional wrongdoing.[90] Accordingly in America a person who has not acted with intention would not contravene rule 10*b*-5 of the Securities Exchange Act of 1934.

It is submitted that the interpretation of the words 'manipulative' and 'deceptive' by the American Supreme Court would be persuasive authority for the interpretation of these terms under the SSA since the wording of s 75(1)(*a*) of the SSA is similar to that of rule 10*b*-5 of the Securities Exchange Act of 1934. It is accordingly arguable that the words 'manipulative' and 'deceptive' are 'fault' words that warrant an interpretation that mens rea is required under s 75(1)(*a*) of the SSA, in accordance with the maxim 'actus non facit reum nisi mens sit rea', and that strict liability cannot be imposed under s 75(1)(*a*).

It may be difficult to obtain direct evidence in the form of documents or testimony that a person has used, or has knowingly participated in, a prohibited trading practice.[91] It is more likely that proof of market manipulation would be based on circumstantial or indirect evidence and inferences based on such evidence.[92] In *Herman & MacLean v Huddleston*,[93] the American Supreme Court observed that proof of intention in the context of market manipulation is often a matter of inference from circumstantial evidence and it stated that in this context circumstantial evidence is permissible. For instance, such inferences could be based on patterns of

contravention of the rules and regulations prescribed by the Securities and Exchange Commission. Rule 10b-5 of the Securities Exchange Act of 1934 states the following:

> '**Employment of Manipulative and Deceptive Devices**
> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
> (*a*) to employ any device, scheme or artifice to defraud,
> (*b*) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
> (*c*) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
> in connection with the purchase or sale of any security.'

Market manipulation in the US is also regulated by § 9(*a*) of the Securities Exchange Act of 1934 (15 USC §78*i*), which contains various prohibitions against the manipulation of securities prices in transactions relating to the purchase or sale of securities; §17(*a*) of the Securities Exchange Act of 1933 (17 CFR §240.17*a*-5), which is the general anti-fraud provision of that Act in that it prohibits fraudulent conduct, schemes or practices in the offer or sale of any securities; and §15(*c*)(1) of the Securities Exchange Act of 1934 (15 USC §78*o*(*c*)(1)), which contains anti-fraud provisions relating to broker-dealers.

[88] Supra note 12.

[89] At 194 n12. See also *Basic Inc v Levinson* 485 US 224 (US SC, 1988) at 231.

[90] At 214.

[91] See the Technical Committee of the International Organization of Securities Commissions op cit note 23 at 21.

[92] See *Herman & MacLean v Huddleston* 459 US 375 (US SC, 1983) at 391; Technical Committee of the International Organization of Securities Commissions op cit note 23 at 21.

[93] Supra note 92 at 391, and approved in *In re Software Toolworks, Inc Securities Litigation* 50 F 3d 615 (9th Cir, 1994) at 627.

conduct, the fact that the offender has a pecuniary interest in a security, or could be drawn by analysing the trading patterns and any irregularities which may emerge from the trading data.[94]

4.1.3 'On behalf of another person, directly or indirectly'

Section 75(1)(*a*) of the SSA prohibits a person from using or knowingly participating in a prohibited trading practice 'either for such person's own account or on behalf of another person, directly or indirectly'. The word 'indirectly' implies that if a person engages in a manipulative trading practice via an intermediary, such person would contravene s 75(1)(*a*). The inclusion of the word 'indirectly' prevents a person from circumventing the prohibition of market manipulation by employing some other person to engage in it. It follows from the words 'on behalf of another person' that the intermediary would also be guilty of infringing s 75(1)(*a*), provided that the necessary mens rea element is satisfied. If an intermediary merely executes a customer's order and is ignorant of the fact that the instruction would result in market manipulation, the intermediary would clearly not be guilty of knowingly participating in the manipulative trading practice. This raises the question whether an intermediary is under a duty to satisfy himself or herself that the customers' transactions would not give rise to behaviour that is tantamount to market manipulation. The Financial Services Authority has expressed the view that an intermediary would indeed be expected to make an assessment of the behaviour of the customer and of the nature of the transaction in question in order to determine whether or not this would constitute market manipulation.[95]

The words 'directly or indirectly' were interpreted by the American Supreme Court in *Central Bank of Denver v First Interstate Bank of Denver*,[96] where, in a private cause of action, these words were held not to extend to persons who did not directly engage in manipulative trading practices and who had simply aided and abetted another in the commission of a manipulative or deceptive act.[97] The Court ruled that to impose liability for aiding and abetting would extend beyond persons who engage, even indirectly, in a proscribed activity, to include those persons who did not engage in the proscribed activities but who had merely given some assistance to those who did.[98] Importantly, the Court added the vital caveat that the absence of an aiding and abetting liability in rule 10*b*-5 of the Securities Exchange Act of 1934 did not necessarily mean that secondary actors in the securities markets were free from liability since a secondary actor could be

[94] See the Technical Committee of the International Organization of Securities Commissions op cit note 23 at 21.
[95] See Financial Services Authority Consultation Paper 59 *Market Abuse: A Draft Code of Market Conduct* (Jul 2000) in par 6.87.
[96] Supra note 12.
[97] Idem at 191.
[98] Idem at 176.

liable as a *primary violator* under rule 10*b*-5 if all the requirements for primary liability under this rule were met.[99]

Furthering or assisting the commission of a crime by another can take various forms, such as facilitating a crime, encouraging the commission of a crime, or even simply giving advice.[100] The traditional terminology for such assistance in South African law was 'aids, abets, counsels or assists in the crime'.[101] If the interpretation of the words 'directly or indirectly' in *Central Bank of Denver* were to be applied to s 75(1)(*a*) of the SSA, it would mean that secondary actors – such as investment bankers, accountants, lawyers or underwriters who aid or give assistance to market manipulators that enables a manipulative trading practice, such as advising a client on a business transaction or drafting documents related to a business structure that has questionable business or accounting practices[102] – would not contravene s 75(1)(*a*) unless liability as a primary actor could be pinned on them.

But s 75(1)(*a*) of the SSA differs from rule 10*b*-5 of the Securities Exchange Act of 1934 in an important respect: it prohibits a person from *participating* in a manipulative trading practice. It is submitted that the word 'participate' in s 75(1)(*a*) indicates that a secondary actor who gives some degree of aid or assistance to a market manipulator would be guilty of contravening the section, provided he or she had the necessary mens rea at the time of the participation. For this reason it is submitted that the meaning of the words 'directly or indirectly' as adopted in *Central Bank of Denver* ought not to be applied to the interpretation of these words in s 75(1)(*a*). The difficulty remains of having to distinguish the degree of participation before the offence can be said to have been committed by the secondary actor in question. Would it suffice if the participation were minimal or would substantial participation be required?

As a result of the decision in *Central Bank of Denver*, American courts have not been able to agree on the threshold required for a secondary actor's conduct to implicate primary liability.[103] Two competing tests have developed: the 'substantial participation' test and the 'bright line' test.[104]

According to the substantial participation test, a secondary actor would be liable under rule 10*b*-5 if he or she substantially participated in the practice in question.[105] For instance, in *In re Software Toolworks, Inc Securities Litigation*,[106] the Court held an accounting firm liable as a primary violator of rule 10*b*-5 because of its 'significant role in drafting and editing' a letter sent by its client to the Securities and Exchange Commission, even though the

[99] Idem at 191.
[100] Burchell & Milton op cit note 78 at 600.
[101] *R v Peerkhan & Laloo* 1906 TS 798 at 802.
[102] Tracy Crum 'Unsettled Law of Secondary Actor Liability under Rule 10b-5 Raises Concerns for Attorneys – Part II' (Nov 2006) 14 *The Metropolitan Corporate Counsel* 5, available at *http://www.metrocorpcounsel.com/pdf/2006/November/05.pdf* (last consulted on 17 Mar 2008) at 5.
[103] *Wright v Ernst & Young LLP* 152 F 3d 169 (2d Cir, 1998) at 174.
[104] At 175.
[105] Ibid.
[106] Supra note 93.

accounting firm had not signed or issued the letter.[107] In contrast, the bright line test would impose liability under rule 10*b*-5 on a secondary actor only if he or she had made a false statement or omission on which the plaintiff had relied.[108] For instance, in *Shapiro v Cantor*,[109] on similar facts, the Court held that an accounting firm which had participated in providing financial projections in the preparation of its client's offering memorandum that had contained false statements, could not be held liable under rule 10*b*-5 because it had not issued an opinion nor made a false statement as to the offering memorandum. Most American courts have preferred the bright line test over the substantial participation test on the ground that it is much too difficult to distinguish primary liability from the aiding and abetting liability under the substantial participation test.[110]

Soon after the decision in *Central Bank of Denver,* the American Congress was concerned that the ruling in that case, which applied to private actions, would be extended to prohibit the Securities and Exchange Commission from pursuing *criminal actions* against aiders and abettors.[111] Consequently, s 20(*e*) of the Securities Exchange Act of 1934 was enacted. This section specifically authorises the Securities and Exchange Commission to institute criminal actions for aiding and abetting against 'any person that knowingly provides substantial assistance to another person' who commits a securities-law violation. Thus, while plaintiffs could no longer institute a private action in America for aiding and abetting, the Securities and Exchange Commission could institute criminal actions against secondary actors who knowingly provided substantial assistance to another person who engages in market manipulation.[112]

As to the degree of participation that would be necessary before s 75(1)(*a*) of the SSA may be said to have been contravened by a secondary actor, it is submitted that since the section specifically prohibits 'participation' in a manipulative trading practice, a test similar to the American substantial participation test ought to be applied. If a secondary actor were to incur liability under s 75(1)(*a*) for minimal participation in the offence, it would introduce potentially far-reaching duties and uncertainties for those secondary actors engaged in their clients' day-to-day business transactions.[113] The

[107] At 628.

[108] *Wight v Ernst & Young* supra note 103 at 174-5.

[109] 123 F 3d 717 (2d Cir,1997) at 721.

[110] See Tracy Crum 'Unsettled Law of Secondary Actor Liability under Rule 10b-5 Raises Concerns for Attorneys – Part I' (Oct 2006) 14 *The Metropolitan Corporate Counsel* 17, available at *http://www.metrocorpcounsel.com/pdf/2006/October/17.pdf* (last consulted on 17 Mar 2008) at 17. See, eg, *Wright v Ernst & Young* supra note 103 and *Anixter v Home-Stake Production Company* 77 F 3d 1215 (10th Cir, 1996) at 1226-7.

[111] Matthew L Mustokoff 'Proving Scienter in SEC Aiding and Abetting Cases: Courts Apply Tougher Standard in Recent Decisions' (1 May 2006) *Insights: The Corporate & Securities Law Advisor*, available at *http://www.accessmylibrary.com/coms2/summary_0286-17633449_ITM* (last consulted on 17 Mar 2008).

[112] Ibid.

[113] See *In re Charter Communications Inc Securities Litigation v Scientific-Atlanta, Inc; Motorola, Inc* 443 F 3d 987 (8th Cir, 2006) at 992-3.

substantial participation test would also be consistent with s 20(*e*) of the Securities Exchange Act of 1934, which makes it an offence for a person to 'knowingly provide substantial assistance' to another person in a criminal offence.

4.1.4 False or Deceptive Appearance of Trading Activity

Creating a false or deceptive appearance of a trading activity in connection with a security means that the trading practice engaged in must give a false or deceptive impression as to the supply of or demand for that security.[114] The false trading practice need only create the false *appearance* of trading; it need not actually have had the defined effect.[115] The words 'might create' in s 75(1)(*a*) indicate that the offence would be committed even if a false or deceptive appearance of the trading activity in connection with a security or an artificial price for that security was not in fact created; it is sufficient if the trading practice had the potential to create such an effect.

4.1.5 Artificial Price

The Financial Services Authority in the United Kingdom has issued a Code containing useful guidance on whether or not behaviour amounts to market abuse. It is referred to as the 'Code of Market Conduct'.[116] This Code describes behaviour that, in the opinion of the Financial Services Authority, does or does not amount to market manipulation and it also sets out the factors to be taken into account in determining whether or not a particular behaviour amounts to market manipulation.[117] Some of the factors set out in the Code of Market Conduct as a guide to determining whether or not a person's behaviour amounts to securing the price of an investment at an artificial level, are the extent to which the person had a direct or indirect interest in the price or value of the qualifying investment;[118] the extent to which price, rate or

[114] See s 118(5)(*a*) of the Financial Services and Markets Act, 2000, which prohibits conduct equivalent to that prohibited by s 75(1)(*a*) of the SSA.

[115] *North v Marra Developments Ltd* supra note 37 at 59.

[116] The Code of Market Conduct, which was revised on 1 Jul 2005, was enacted in accordance with s 119 of the Financial Services and Markets Act, 2000. It is known by the abbreviation 'MAR'.

[117] The Code of Market Conduct is not an exhaustive statement of behaviour which amounts to market manipulation (see MAR 1.1.7G). The fact that a particular behaviour is not referred to in the Code does not necessarily mean that such behaviour does not constitute market manipulation: see *Gower & Davies Principles of Modern Company Law* 7 ed by Paul L Davies (2003) at 785. The Code plays an important role in regulating market abuse in the UK because where it indicates that a certain type of behaviour does not constitute market manipulation, this is conclusive, and where it indicates that a certain type of behaviour would constitute market manipulation, this may be relied on in an action brought by the Financial Services Authority. It goes further than many statutory provisions relating to codes of practice in other disciplines which usually require that a code merely be taken into account by the adjudicatory body: see Gower & Davies op cit at 784.

[118] 'Qualifying investments' are the investments set out in art 5 of the Financial Services and Markets Act, 2000 (Prescribed Markets and Qualifying Investments) Order, 2001 (SI 2001/996). The qualifying investments comprise those financial instruments defined in art 1(3) of the EU Market Abuse Directive. They include shares, bonds, units in collective investment undertakings, money-market instruments, financial-futures contracts, forward interest rate agreements, interest-rate, currency and equity swaps, derivatives on commodities, and options to acquire or dispose of any instrument falling into these categories.

option volatility movements for the investment in question are outside their normal daily, weekly or monthly range; and whether a person has successively and consistently increased or decreased his or her bid, offer or the price he or she has paid for a qualifying investment.[119] It is submitted that these factors would be equally applicable in the case of s 75(1)(*a*)(*ii*) of the SSA in determining whether a trading practice has created an artificial price for a security.

4.1.6 Placing Orders to Buy or Sell Listed Securities

Section 75(1)(*b*) of the SSA makes it an offence for a person to place an order to buy or sell listed securities which, if executed, would, to his or her knowledge, create, or might create, a false or deceptive appearance of the trading activity in connection with that security or an artificial price for that security. The word 'knowledge' in s 75(1)(*b*) indicates that the fault element required is that of intention.[120] Article 1(2)(*a*) of the EU Market Abuse Directive contains a similar prohibition.

Unlike s 75(1)(*a*), s 75(1)(*b*) does not make it an offence to place an order to buy or sell securities 'directly or indirectly'. The question must therefore arise whether one would infringe s 75(1)(*b*) if one instructed an intermediary to place an order to buy or sell securities which would have the effect contemplated in s 75(1)(*a*). It is submitted that even though the word 'indirectly' is not expressly used in subs (*b*), the provision would nevertheless be contravened in this scenario as one's instructions to the intermediary could arguably constitute the placing of an order to buy or sell securities. The offence would be committed when the intermediary is instructed to place the relevant order on one's behalf.

Significantly, s 75(1)(*b*) does not make it an offence for one to place an order 'on behalf of another person', as is the case with s 75(1)(*a*). This could be the result of an oversight on the part of the Legislature. The question thus arises whether an intermediary who was instructed to place an order to buy or sell listed securities on behalf of another person would escape liability under s 75(1)(*b*). It is once again submitted that the answer depends on the knowledge of the intermediary, namely whether the intermediary knew that the placing of the order would have the effect contemplated in s 75(1)(*a*). Clearly where one colludes with one's intermediary, the intermediary would infringe s 75(1)(*b*) by placing the order on one's behalf.[121] Again, the question must arise whether intermediaries have any duty to satisfy themselves that the placing of their customers' orders would not give rise to behaviour that amounts to market manipulation. It is submitted on principle that intermediaries ought to be required to make an assessment of the behaviour of their

[119] See MAR 1.6.10E.
[120] See Burchell & Milton op cit note 78 at 501.
[121] See the Draft Code of Market Conduct op cit note 95 in par 6.87.

customers and of the nature of the transaction in question in order to determine whether or not this would constitute market manipulation.

4.1.7 Regulated Market

The prohibition in s 75(1)(*a*) of the SSA against engaging in a prohibited trading practice relates to securities[122] 'listed[123] on a regulated market.' Section 72 defines a 'regulated market' as meaning 'any market, whether domestic or foreign, which is regulated in terms of the laws of the country in which the market conducts business as a market for dealing in securities listed on that market'. This clearly means that the market manipulation provisions of the SSA would apply to securities listed on a foreign market, even if there is no territorial link to South Africa, just as it does in the case of insider trading.[124]

In contrast, art 10 of the EU Market Abuse Directive requires Member States to apply its provisions to 'actions carried out in its territory or abroad concerning financial instruments admitted to trading on a regulated market[125] situated or operating within its territory or for which a request for admission to trading on such market has been made'. This allows Member States to apply the market manipulation rules to securities transactions taking place outside Europe provided the market manipulation in question concerns securities admitted to trading on a regulated market in their State.[126] In other words, unlike our statutory provisions, a territorial nexus must exist with the Member State concerned.

Similarly in the United Kingdom, behaviour would constitute market manipulation in terms of the Financial Services and Markets Act, 2000, if it occurs in the United Kingdom or in relation to qualifying investments which are admitted to trading (or for which a request has been made for admission to trading) on a prescribed market situated or operating in the United

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[122] The definition of 'securities' is set out in s 1 of the SSA. Money market instruments have been expressly excluded from the definition (except for the purposes of ch IV of the SSA, which deals with the custody and administration of securities).

[123] 'Listed securities' are defined in s 1 of the SSA as meaning 'securities included in the list of securities kept by an exchange in terms of section 12'. An 'exchange' is defined in s 1 as meaning 'a person who constitutes, maintains and provides an infrastructure – (*a*) for bringing together buyers and sellers of securities; (*b*) for matching the orders for securities of multiple buyers and sellers; and (*c*) whereby a matched order for securities constitutes a transaction.' A 'transaction' is a contract of purchase and sale of securities (s 1).

[124] See PC Osode 'The New South African Insider Trading Act: Sound Law Reform or Legislative Overkill?' (2002) 45 *J of African Law* 239 at 260, and Cassim op cit note 11 at 66-7.

[125] A 'regulated market' is defined in art 1(4) of the EU Market Abuse Directive as meaning a market as defined by art 1(13) of Council Directive 93/22/EEC of 10 May 1993 on Investment Services in the Securities Field (*Official J* L141 of 11 Jun 1993). Article 1(13) defines a 'regulated market' as a market for the instruments listed in Section B of the Annex to the directive which appears on a list of regulated markets required to be drawn up by each Member State in terms of art 16 of the Directive. These instruments include shares, bonds, units in collective investment undertakings, money-market instruments, financial-futures contracts, forward interest rate agreements, interest-rate and currency and equity swaps.

[126] See Eric Cafritz & Olivier Genicot 'EU Market Abuse Rules' (3 Dec 2004), available at *http://www.ffhsj.com/siteFiles/Publications/3212AC6C244C3C9F6E0F0D159545BF58.pdf* (last consulted on 17 Mar 2008), at 2.

Kingdom.[127] The Financial Services Authority may act only if either the behaviour occurs in the United Kingdom or the instrument affected is traded there (or has been requested to be traded there).[128] In other words, in order for the Financial Services Authority to assert jurisdiction under the Financial Services and Markets Act, 2000, there must once again be a territorial nexus with the United Kingdom.

It is rather strange that the SSA should not require any territorial link with South Africa for a market manipulation offence to be committed under the SSA. It is submitted that if manipulative behaviour occurs outside South Africa but would affect a South African financial market, the FSB is rightly granted jurisdiction to investigate and pursue such conduct. But it is not clear how the South African financial markets would benefit from a prosecution of a non-resident who manipulates a foreign market where this has no effect on a South African financial market.[129] In any event, the cost of pursuing such a prosecution on a global scale would undoubtedly be prohibitive.[130]

4.2 Deemed Prohibited Trading Practices

Section 75(3) of the SSA deems certain trading practices to be manipulative, improper, false or deceptive. If an activity meets the requirements of a deemed manipulative trading practice, that activity will be deemed to have infringed s 75(1) of the SSA. The use of the words 'without limiting the generality of subsection (1)' in s 75(3) make it clear that if an activity does not meet the requirements of a deemed manipulative trading practice, it may still be prohibited if it infringes the general prohibition contained in s 75(1). Some of the trading practices that are deemed to be manipulative, improper, false or deceptive create a false or deceptive appearance of the trading activity in connection with the security, while other trading practices create an artificial price for that security.

4.2.1 Wash Sales

Section 75(3)(*a*) deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*a*) Approving or entering on a regulated market an order to buy or sell a security listed on that market which involves no change in the beneficial ownership of that security'.

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[127] Section 118A(1) of the Financial Services and Markets Act, 2000.

[128] See Alistair Alcock 'Five years of Market Abuse' (2007) 28 *The Company Lawyer* 163 at 166. Where trading on a European Economic Area exchange takes place from the UK, the market manipulation regimes of both the UK and the other European Economic Area jurisdiction will apply. The implication of the extra territorial effect is that an offender may face investigation by a regulator in more than one country. Co-operation would thus be necessary between the regulators: see Recital 40 to the EU Market Abuse Directive; Practical Law Company Practice Note 'Market Abuse: The 1 July 2005 Regime' (25 Apr 2006), available at *http://www.practicallaw.com/8-200-8043* (last consulted on 4 Dec 2007) at 7.

[129] Osode op cit note 124 at 260.

[130] Ibid.

This practice is known as a 'wash sale'.[131] It involves a person, either directly or indirectly being both the purchaser and the seller of securities in the same transaction, with the result that the purchaser incurs no real financial obligation to the seller and there is no change in the beneficial ownership of the security.[132] A wash sale creates a false or deceptive appearance of trading activity in connection with a security. The manipulator undertaking a wash sale usually undertakes frequent trades in the security in the hope that other investors would be attracted by the increased turnover of the security.[133] The object of this practice is to gain financially by creating a small price differential between the buy and sell rates of the security in question.[134] In *United States v Brown*,[135] the Court remarked that wash sales are in the nature of deceit as they 'broadcast the fact that a buyer and a seller have agreed to exchange the shares at a published price, when they have not done so'.

The term 'beneficial ownership' is not defined in the SSA, but the Listings Requirements of the JSE Securities Exchange[136] defines 'beneficial owner' as meaning, in relation to a security, 'the de facto right or entitlement to receive any dividend or interest payable in respect of that security; or the de facto right to exercise or cause to be exercised in the ordinary course of events, any or all of the voting, conversion, redemption or other rights attached to such security'. Section 75(4) of the SSA spells out when a purchase or sale of listed securities will not involve a change in the beneficial ownership:

> 'A purchase or sale of securities listed on a regulated market does not, for the purposes of subsection 3*(a)*, involve a change in the beneficial ownership if a person who has a beneficial interest in those securities before the purchase or sale, or a person associated with that person in relation to those securities, directly or indirectly holds a beneficial interest in those securities after the purchase or sale.'

Section 75(4) of the SSA does not define the phrase 'a person associated with that person'. However, the section corresponds, almost verbatim to s 1041B(3) of the Australian Corporations Act, 2001, which does define the term 'associates'. Under the Australian Act, 'associates' include a director or secretary of the company, a related company and a director or secretary of the related company; a person in concert with whom the person is acting or proposes to act; a person with whom the person is or proposes to become associated in any way, and a person with whom the person has entered into

[131] Section B of the Annex to the Proposal for a Directive of the European Parliament and of the Council on insider dealing and market manipulation (market abuse), COM (2001) 281 final – 2001/0118/(COD) (1 Jun 2001) (the 'EU Market Abuse Proposal'); *Ernst & Ernst v Hochfelder* supra note 12 at 205 n25.

[132] NZ Ministry of Economic Development op cit note 3 in par 73; Ali op cit note 6 at 223.

[133] NZ Ministry of Economic Development op cit note 3 in par 73.

[134] Ibid.

[135] 79 F 2d 321 (2d Cir, 1935) at 325. Section 75(3)(*a*) of the SSA corresponds to §9(*a*)(1)(*A*) of the Securities Exchange Act of 1934, which makes it unlawful to effect a transaction in a security which involves no change in the beneficial ownership thereof, for the purpose of creating a false or misleading appearance of active trading in any security registered on a national securities exchange, or a false or misleading appearance with respect to the market for any such security.

[136] The 'JSE Listings Requirements'.

any transaction or does or proposes to do any act or thing with a view to becoming associated with that person.[137]

The JSE Listings Requirements[138] define the term 'associate' as including, in relation to an *individual*, the individual's immediate family; the trustees of any trust of which the individual or his immediate family is a beneficiary or discretionary subject; and a company in which equity securities the individual or any person or trust so contemplated, taken together, are directly or indirectly beneficially interested, or have a conditional, contingent or future entitlement to become beneficially interested, and the individual or any person or trust so contemplated would on the fulfilment of the condition or the occurrence of the contingency be able to exercise or control the exercise of 35 per cent or more of the votes able to be cast at general meetings on all or substantially all matters, or to appoint or remove directors holding 35 per cent or more of the voting rights at board meetings on all or substantially all matters. In relation to a *company*, an associate is defined in the JSE Listings Requirements as including any other company that is its subsidiary, holding company or subsidiary of its holding company; any company whose directors are accustomed to act in accordance with the company's directions or instructions; and any company in the capital of which the company, and any other company contemplated above taken together, is, or would on the fulfilment of a condition or the occurrence of a contingency, be able to exercise or control the exercise of 35 per cent or more of the votes able to be cast at general meetings on all or substantially all matters, or appoint or remove directors holding 35 per cent or more of the voting rights at board meetings on all or substantially all matters.

It is not clear if the definition of 'associate' in the JSE Listings Requirements is to be applied to s 75(4) of the SSA, but it is submitted that the definition is certainly wide enough to prevent the mischief at which s 75(3)(*a*) is aimed.

4.2.2 Matched Orders

Section 75(3)(*b*) of the SSA deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*b*) approving or entering on a regulated market an order to buy or sell a security listed on that market with the knowledge that an opposite order or orders of substantially the same size at substantially the same time and at substantially the same price, have been or will be entered by or for the same or different persons with the intention of creating –
> (*i*) a false or deceptive appearance of active public trading in connection with, or
> (*ii*) an artificial market price for,
> that security'.[139]

This practice, known as a matched order,[140] creates a false or deceptive appearance of the trading activity in connection with a security as well as an

[137] See ss 10-17 of the Australian Corporations Act, 2001.
[138] In its definitions section.
[139] Section 9(*a*)(1)(*B*) and (*C*) of the Securities Exchange Act of 1934 contain a similar prohibition.
[140] See *Ernst & Ernst v Hochfelder* supra note 12 at 205n25.

artificial price for that security. It occurs when a person buys a security with a low turnover and subsequently places contemporaneous buy and sell orders for that security, which are for substantially the same size and price, and occur at substantially the same time.[141]

The main objective of this practice is to create or convey an appearance of renewed interest in the security in question in order to induce others to purchase the security, in the hope that if a sufficient number of new investors are attracted by the apparent increase in trading activity, the price of the security would rise.[142] Should this occur, the manipulator would then sell the security at a profit.[143]

A 'pool' is essentially a similar kind of practice as a matched order, but with the difference that it involves a group of persons combining their resources to buy shares and then to sell them successively from one member of the group to another in order to boost the turnover in the shares.[144]

4.2.3 Buying Orders at Successively Higher Prices and Selling at Successively Lower Prices

Section 75(3)(*c*) of the SSA deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*c*) approving or entering on a regulated market orders to buy a security listed on that market at successively higher prices or orders to sell a security listed on that market at successively lower prices for the purpose of unduly or improperly influencing the market price of such security'.

This section prohibits the entering of orders on a regulated market at prices which are higher than previous prices or lower than previous prices with the object of improperly creating an artificial price for that security. This practice

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141 See NZ Ministry of Economic Development op cit note 3 in par 71. In the first case of market manipulation under the SSA to be heard publicly, the FSB accused a certain hedge-fund manager of two instances of market manipulation dating back to Mar 2005. In the first instance he was accused of conducting a market-manipulation scheme in terms of which he placed an order at the end of Mar 2005 to sell 500 shares of SA Retail Properties Ltd at R8.75 each on behalf of his company, Velocity Trading (Pty) Ltd, and on the same day placed an order on behalf of the Mayibentsha Fund, for whom he also managed funds, to buy the same number of shares of SA Retail Properties at the same price. The FSB alleged that his purpose was to inflate the closing price of the shares of SA Retail Properties in the hope of inflating the value of his clients' portfolio at the close of the quarterly reporting window: a classic case of 'window dressing'. The second manipulative trading practice was that of entering orders into the market, at the end of Mar 2005, to buy shares of iFour Properties Ltd at prices of up to R9.40 each, even though the last traded price of the shares at the time was R8.70. The FSB was of the view that the order was placed in this manner in order to 'bid up' the price of shares of iFour Properties so as to make his clients' portfolios look more impressive than they actually were. It was reported that the FSB intended to impose a fine of R10m for these offences if the fund manager was found guilty. See the report by Rob Rose 'FSB Flexes New Muscle' 10 Aug 2007 *Financial Mail* at 21, and by Gareth Stokes 'Make Sure the Punishment Fits the Crime' 14 Aug 2007 *FA News*, available at *http://www.fanews.co.za/article.asp?Compliance_Regulatory;2,FSB;1059,Make_sure_the_punishment_fits_the_crime;2783* (last visited on 17 Mar 2008).

142 See NZ Ministry of Economic Development op cit note 3 in par 71.

143 Ibid.

144 Idem in par 72; Ali op cit note 6 at 223; Black op cit note 27 at 994.

has the effect of creating the misleading impression that there is a demand for or supply of the security in question at that price.[145]

4.2.4 Marking the Close

Section 75(3)(*d*) of the SSA deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*d*) approving or entering on a regulated market an order at or near the close of the market, the primary purpose of which is to change or maintain the closing price of a security listed on that market'.

This practice is known as 'marking the close' and it is a time-specific trade-based activity.[146] The aim of buying or selling the securities at the close of the market is to alter the closing price of the securities and so to mislead persons acting on the basis of the closing prices.[147] This might be done in order to support a flagging price or to artificially affect the valuation of a portfolio, which is known as 'window dressing'.[148] Since the market price is pushed to a distorted level, this practice creates a false impression as to the demand for and the price of the securities.[149]

It is important to observe that s 75(3)(*d*) does not as such deem the mere entering of an order on a regulated market at or near the close of the market to be a manipulative trading practice. It is only when the *primary purpose* of doing so is to change or maintain the closing price of the security, that the practice becomes manipulative. One may therefore legitimately enter an order to buy or sell securities at or near the close of the market, provided that one's primary purpose in doing so is not to change or maintain the closing price of that security.[150]

4.2.5 Auctioning Processes or Pre-opening Session

Section 75(3)(*e*) of the SSA deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*e*) approving or entering on a regulated market an order to buy a security listed on that market during any auctioning process or pre-opening session and cancelling such order immediately prior to the market opening, for the purpose of creating or inducing a false or deceptive appearance of demand for or supply of such security'.

This practice has the obvious effect of creating a false or deceptive appearance of the trading activity in connection with a security. In an auction market, the placing of bids, even if they are never met by sellers, may as

[145] See MAR 1.6.2E.
[146] See Section B of the Annex to the EU Market Abuse Proposal.
[147] Ibid.
[148] See NZ Ministry of Economic Development op cit note 3 in par 77.
[149] Ali op cit note 6 at 222.
[150] See Stephanie Luiz 'Market Abuse II – Prohibited Trading Practices, and Enforcement' (2002) 4 *Juta's Business Law* 180 at 180.

effectively influence the price of a security as a completed sale mainly because it causes other bidders to raise their bids.[151]

Rule 7 of the JSE Equities Rules, which prescribes rules relating to market conduct that are binding on members and their employees,[152] likewise deems an order to buy or sell a security during an auction call period,[153] and the cancelling of such an order immediately prior to the auction matching,[154] for the purpose of creating or inducing a false or deceptive appearance of demand for or supply of such security, a manipulative or deceptive trading practice.[155]

4.2.6 Market Corner

Section 75(3)(*f*) of the SSA deems to be manipulative, improper, false or deceptive the following trading practice:

> '(*f*) effecting or assisting in effecting a market corner'.

'Market corner' is defined in s 72 of the SSA as meaning:

> 'any arrangement, agreement, commitment or understanding involving the purchasing, selling or issuing of securities listed on a regulated market –
> (*a*) by which a person, or a group of persons acting in concert, acquires direct or indirect beneficial ownership of, or exercises control over, or is able to influence the price of, securities listed on a regulated market; and
> (*b*) where the effect of the arrangement, agreement, commitment or understanding is or is likely to be that the trading price of the securities listed on a regulated market, as reflected through the facilities of a regulated market, is or is likely to be abnormally influenced or arbitrarily dictated by such person or group of persons in that the said trading price deviates or is likely to deviate materially from the trading price which would otherwise likely have been reflected through the facilities of the regulated market on which the particular securities are traded'.

A market corner arises where a person, or group of persons acting in concert, buys up a substantial volume of a security, knowing that other market participants would be forced to buy from him, or them, at a higher price.[156] A similar practice is known as an 'abusive squeeze', and arises where a person has a dominant position in the market and then seeks to use his or her control or influence to cause a shortage and so to create artificial prices.[157] Having a substantial influence over supply and extracting elevated profits thereby is not

[151] See Nancy Toross 'Double-Click on This: Keeping Pace with On-Line Market Manipulation' (1999) 32 *Loyola of Los Angeles LR* 1399 at 1413.

[152] See rule 2.30.2.1 of the JSE Equities Rules.

[153] An 'auction call period' is defined in rule 1.40 of the JSE Equities Rules as meaning 'a period of time during which orders for inclusion in an auction can be entered into and deleted from the central book order and there is no automated trading. 'Automated trade' is a transaction which is matched automatically in the JSE equities trading system during continuous trading: see rule 1.40 of the JSE Equities Rules.

[154] 'Auction matching' is defined in rule 1.40 of the JSE Equities Rules as meaning 'the process of matching buy and sell orders according to a matching algorithm at the end of an auction call period'.

[155] See rule 7.10.4.1.4 of the JSE Equities Rules.

[156] See NZ Ministry of Economic Development op cit note 3 in par 75.

[157] See Kern Alexander 'Insider Dealing and Market Abuse: The Financial Services and Markets Act 2000' (2001) ESRC Centre for Business Research, University of Cambridge, Working Paper No 222, available at *http://www.cbr.cam.ac.uk/pdf/WP222.pdf* (last consulted on 17 Mar 2008).

of itself abusive; the abuse lies in cornering the market and then using it to distort the market.[158]

4.2.7 Maintaining an Artificial Price

Section 75(3)(*g*) of the SSA deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*g*) maintaining at a level that is artificial the price for dealing in securities listed on a regulated market'.

This is a general prohibition on a practice that has the effect of creating an artificial price for a security. It appears to be a repetition of s 75(1)(*a*)(*ii*) which prohibits a person from using or knowingly participating in a manipulative, improper, false or deceptive trading practice that creates an artificial price for a security, but it is in fact wider since all that needs to be proved for this section to be contravened is that a person maintained the price of a listed security at an artificial level. It is not necessary to prove that the person intended to do so, as is the position under subs (1)(*a*)(*ii*). Furthermore, the latter subs prohibits the creation of an artificial price, whereas s 75(3)(*g*) prohibits the maintaining of an artificial price for dealing in a listed security. A similar practice was prohibited by s 20(*b*)(*ii*) of the Financial Markets Control Act of 1989.

4.2.8 Manipulating Devices, Schemes or Artifices

Section 75(3)(*h*) of the SSA deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*h*) employing any device, scheme or artifice to defraud any other person as a result of a transaction effected through the facilities of a regulated market'.

The prohibition that was contained in s 20(*c*) of the Financial Markets Control Act of 1989 had prohibited the use of a fictitious or artificial transaction or device in order to maintain, inflate, depress or cause fluctuations in the price for dealing in financial instruments on a financial market. It is now contained in s 75(3)(*h*). The wording of subs (3)(*h*) is substantially the same as that contained in rule 10*b*-5(*a*) of the Securities Exchange Act of 1934, which provides that it shall be unlawful to 'employ any device, scheme or artifice to defraud,' in connection with the purchase or sale of any security. The wording of s 75(3)(*h*) corresponds broadly to that contained in §10(*b*) of the Securities Exchange Act of 1934,[159] s 118(6) of the Financial Services and Markets Act, 2000,[160] and art 1(2)(*b*) of the EU Market

[158] See Alistair Alcock 'Market Abuse' (2002) 23 *The Company Lawyer* 142 at 145.

[159] Section 10(*b*) of the Securities Exchange Act of 1934 prohibits the use of 'any manipulative or deceptive device' in connection with the purchase or sale of a security.

[160] Section 118(6) of the Financial Services and Markets Act, 2000, provides that '[t]he fifth [type of behaviour] is where the behaviour consists of effecting transactions or orders to trade which employ fictitious devices or any other form of deception or contrivance'.

Abuse Directive.[161] The drafters of §10(*b*) of the Securities Exchange Act of 1934 described the measure as a 'catchall' clause to enable the Securities and Exchange Commission to 'deal with new manipulative devices.'[162] This view of §10(*b*) was approved in *Ernst & Ernst v Hochfelder*.[163] It is submitted that s 75(3)(*h*) could likewise be seen as a catch-all provision in terms of which new devices, schemes or artifices may be regulated.

For the purposes of applying art 1(2)(*b*) of the EU Market Abuse Directive, art 5 of Commission Directive 2003/124/EC[164] sets out two non-exhaustive signals that are to be taken into account in determining whether the transactions or orders to trade have employed fictitious devices or other forms of deception or contrivance. The first signal is where orders to trade given or transactions undertaken by persons are preceded or followed by the dissemination of false or misleading information by the same persons or persons linked to them. The second is where orders to trade are given or transactions are undertaken by persons before or after the same person or persons linked to them produce or disseminate research or investment recommendations which are erroneous or biased or demonstrably influenced by a material interest. For instance, where a person takes advantage of occasional or regular access to traditional or electronic media by expressing an opinion about a security while having previously taken a position on that security and profiting subsequently from the impact of those expressed opinions on the price of that security, without having simultaneously disclosed the conflict of interest to the public in a proper and effective way, that person will be held to have employed a manipulative device.[165]

4.2.9 Engaging in Any Manipulative Act, Practice or Course of Business

Section 75(3)(*i*) of the SSA deems the following practice to be a manipulative, improper, false or deceptive trading practice:

> '(*i*) engaging in any act, practice or course of business in respect of dealings in securities listed on a regulated market which is deceptive or which is likely to have such effect'

[161] One element of the definition of market manipulation in art 1(2)(*b*) of the EU Market Abuse Directive is 'transactions or orders to trade which employ fictitious devices or any other form of deception or contrivance.'

[162] See the statement of Thomas G Corcoran, a spokesperson for the drafters of the Securities Exchange Act of 1934, in relation to §9(*c*) of the Bill which became the Securities Exchange Act of 1934, and which § later became §10(*b*) of the Securities Exchange Act of 1934, quoted in *Ernst & Ernst v Hochfelder* supra note 12 at 202-3.

[163] See *Ernst & Ernst v Hochfelder* supra note 12 at 203.

[164] See the Commission Directive 2003/124/EC of 22 Dec 2003, implementing Directive 2003/6/EC of the European Parliament and of the Council, as regards the definition and public disclosure of inside information and the definition of market manipulation: *Official J* L339 of 24 Dec 2003.

[165] See MAR 1.7.2E(1).

Section 75(3)(*i*) is worded in almost identical terms to rule 10*b*-5(*c*) of the Securities Exchange Act of 1934.[166] It is a widely worded provision which prohibits any act, practice or course of business in respect of dealings in securities which is deceptive, or is likely to be deceptive.

(To be continued.)

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[166] Rule 10*b*(5)(*c*) of the Securities Exchange Act of 1934 makes it unlawful for a person 'to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person'.