SCWP SCHINDHELM

CROSSINGS & MARKET MANIPULATION: THE RISKS OF "SELF-DEALING"

In recent months, there have been increased reports of fines by private investors on the part of the Financial Market Authority (FMA). The reason for this was repeated cases of market manipulation by means of "crossing".

The most recent sanctioning of this type took place on 29.06.2021 and was directed against a small private investor. After this party concluded various "crossing" trades, the FMA imposed a penalty of EUR 600.00.

The following article is intended to provide a rough overview of "crossings" and the concept of "market manipulation" as characterised by EU law. After that, the legal consequences that can arise due to "crossings" are examined, and finally, tips are given to avoid them.

I. WHAT ARE CROSSINGS AND HOW ARE THEY CARRIED OUT?

"Crossings", "wash trades", and "self-dealing" represent cash flows where the beneficial owner does not change. This phenomenon in securities trading is referred to as "market crossing". Here, the acting person represents both the buyer and the seller of the traded security.

Market participants often are not at all aware that they are concluding a so-called "crossing" and potentially even engaging in sanctioned securities trades. The problem here is the resulting possible market manipulation, which is covered by EU law and can result in consequences under criminal or administrative criminal law.

"Crossings" can occur specifically if the seller of securities immediately attaches an equivalent purchase order with the same security market value to his/her sale. If the sales order has not yet been completed, the seller buys exactly the same security again that he/she sold beforehand. The beneficial owner never changed after the financial trades were concluded. The purchaser is, in fact, also the seller.

In principle, these types of trades do not pose a problem in themselves. However, "crossing" tends to manipulatively affect the capital market, which can result in legal consequences pursuant to the Market Abuse Regulation (MarktmissbrauchsVO) and the Market Abuse Directive (MarktmissbrauchsRL). The boundary between legal and prohibited trades is blurred in the process and presents legal challenges to securities traders.

II. WHAT DO THE MARKET ABUSE REGULATION AND THE MARKET ABUSE DIRECTIVE REGULATE?

Regulation (EU) No. 596/2014 of the European Parliament and of the Council of 16.04.2014 on market abuse (**Market Abuse Regulation**) was issued in order to counteract manipulation of the EU financial markets by deceptive acts and omissions within and outside the inner market. The date of entry into force was 03.07.2016.

The primary goal of the Market Abuse Regulation is to ensure the EU financial markets are completely transparent and free of manipulative activities. Three types of cases of market abuse must be differentiated, namely "market manipulations", "insider trades", and the "illegal disclosure of insider information".

Directive 2014/57/EU of the European Parliament and of the Council of 16.04.2014 on criminal sanctions in market manipulation (**Market Abuse Directive**) was issued at the same time as the Market Abuse Regulation and was also to be implemented by 03.07.2016.

The core content of the Market Abuse Directive includes the mandatory implementation of criminal sanctions for both individuals and legal entities.

These two EU legal provisions work synergistically to maintain the trust of the public in the markets and at the same time set minimum requirements for the EU member states with regard to agency competencies and sanction mechanisms.

III. WHAT LEGAL CONSEQUENCES DO CROSSINGS HAVE?

If a "crossing" results in market manipulation, the act falls within the scope of application of the Market Abuse Regulation and the Market Abuse Directive.

According to Art. 12 of the Market Abuse Regulation and Art. 5 of the Market Abuse Directive, market manipulation exists in all financial trades that send *false or deceptive signals regarding the offer or price of a financial instrument* to the capital market, or for which this is likely. According to Art. 15 of the Market Abuse Regulation, market manipulations and attempts to carry them out are prohibited. In the event of violations of these regulations, proof of intent is not required.

If a "crossing" is carried out now, this can result in market manipulation under certain circumstances, specifically if an increasing demand for the security in question is conveyed to the capital market. If the "crossing" conveys an increased demand, the market usually responds with a price increase.

Art. 7 of the Market Abuse Directive makes provisions for imprisonment of individuals with a maximum term of four years. In addition, pursuant to Art. 30 of the Market Abuse Regulation, Member States shall be granted the authority to impose administrative penalties of up to EUR 5,000,000.00.

Art. 8 of the Market Abuse Directive establishes the minimum penalties for legal entities in the event of an executed market manipulation. The Member States must accordingly impose *effective, proportionate, and deterrent sanctions* and open up the possibility of further consequences such as *exclusion from public benefits, prohibition of engaging in trading activities, placement under judicial supervision, judicial dissolution measures, or permanent closure of establishments*. Under administrative criminal law, penalties in the amount of EUR 15,000,000.00 or 15% of the total annual turnover may be imposed by the Member States in accordance with Art. 30 of the Market Abuse Regulation.

IV. HOW CAN CROSSINGS BE AVOIDED?

To avoid "crossings", the following should be taken into account when concluding securities trades:

1. Make sure your sales order is fully completed to avoid repurchasing the exact same security.
2. Make sure that your share purchases and sales cannot be offset.
3. After selling a security, do not purchase a similar security after trading has closed on

the exchange. You could end up repurchasing the exact same previously sold security at the beginning of the new trading day.

4. Before purchasing a share, check whether there is an offsetting and not yet executed sales order.
5. Purchase the share on an exchange other than the one on which you have previously sold.

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