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Market abuse and commodities

What is market abuse?

The market abuse regime in the UK is enshrined in The Market Abuse (Amendment) (EU Exit) Regulations 2019 (the "**UK MAR**"), which applies to financial instruments admitted to trading or traded on both UK and EU trading venues.

Market abuse is defined as intentional conduct that violates market integrity, the offences in respect of which can be categorised as either civil or criminal. The civil offences include insider dealing, unlawful disclosure, market manipulation and attempted manipulation, which are contained in Articles 14 and 15 of the UK MAR. In the criminal context, insider dealing amounts to a criminal offence under Part V of the Criminal Justice Act 1993, and criminal market manipulation is an offence under sections 89-91 of the Financial Services Act 2012.

The changing Regulatory landscape

The regulatory landscape has resulted in increased scrutiny on the commodities market. New regulations have been introduced and increased enforcement action taken to reduce systemic risk; increase market transparency and integrity; and ultimately deter market participants from committing these offences.

More powers to the regulators

Individual accountability, culture and governance is the latest focal point of the UK's financial regulatory body, the Financial Conduct Authority (the "**FCA**").

On individual accountability, the FCA recently fined three bond traders for alleged market manipulation, with two traders receiving a fine of £100,000 and one receiving a fine of £395,000. It is the FCA's published case that each of the traders placed

misleading orders by repeatedly placing large orders on one side of the order book on an exchange to assist in executing small orders for the same instrument on the other side of the book, and then cancelling the large orders before execution. The FCA have characterised this as a pattern of deliberate and intentional market manipulation, which is "*serious and directly undermin[es] the integrity of the market*".¹

Regarding culture and governance, in a speech in June 2023, the FCA emphasised the importance of cultural changes to meet regulatory expectations, highlighting that "*culture remains central to [the FCA's] supervisory model*", that it is "*what underpins outcomes, [and that] firms with healthy cultures will be best equipped to adapt to a changing world and to consumers with changing expectations*". Moreover, in the FCA's Business Plan for 2023-2024, it is emphasised that firms must have "*the right culture and safeguards in place to spot, report and reduce the risk of market abuse by having robust systems and controls, high-quality reporting practices and a strong anti-market abuse culture*". The FCA highlighted that this will be achieved by a continued coordinated approach across the involved functions within the FCA on very high-risk firms facing multiple regulatory failures, including market abuse, so as to maintain market confidence.

Increase in regulatory sanctions

In addition to the three bond traders recently fined for alleged market manipulation, the FCA recently imposed a fine of £4,775,200 on BGC Brokers LP, GFI Securities Limited and GFI Brokers Limited ("**BGC/GFI**") for a failure to ensure there were adequate risk management surveillance systems for the purposes of detecting and identifying orders and

¹ Each of the three traders has referred its Decision Notice to the Upper Tribunal.

transactions that could constitute insider dealing, market manipulation or attempted insider dealing or market manipulation.

Commodity market abuse has a bearing on the economy

Commodities markets have been impacted significantly by the recent events in Russia and Ukraine, as Russia is a major supplier of oil, natural gas, wheat, nickel, and palladium. Following the Russian invasion, the London Metal Exchange (the "LME") suspended trading in nickel, which is a crucial material for electric car batteries, after prices doubled over the course of a day to a record price of £76,200 per tonne. Though the trading of nickel resumed a week later, the FCA and Bank of England commissioned a review of how the LME handled the suspension, noting that it raises questions on the structure of the market and "*particularly the role of transparency*".²

The importance of market surveillance solutions

With the change in the regulatory landscape comes the need to ensure there are robust market surveillance solutions in place.

For example, in the case of BGC/GFI, it was found that they did not have effective and ongoing monitoring for suspected market abuse that was appropriate, proportionate and effective for the nature, scale and size of orders and transactions undertaken by them and the potential risk of market abuse to which their business was exposed. Particular failings found were, by way of example, the exclusion of certain asset classes that fall within the scope of UK MAR from their automated surveillance system and, where manual surveillance was in place, the use of sample-based reviews was an inadequate approach.³ In relation to market abuse risks, of the six risks set out in UK MAR,⁴ BGC/GFI failed to address these adequately for a number of asset classes, resulting in a risk that suspicions of market abuse would not have been identified and reported in suspicious transaction and order reports.

Thus, it would be prudent to ensure that a firm's market surveillance solutions, whether they are automatic or manual, are extensive and proportionate to the size of the business and the risks to which it is exposed and that all asset classes that fall within UK MAR are fully covered.

Contact us

We hope that you find this update both useful and interesting. If you have any comments or would like to learn more about this topic, please get in touch with either your usual SH contact or any member of our commodities team by clicking [here](#).

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² For more detail see our recent article on this judgment ([here](#))

³ Financial instruments are listed in Part 1 of Schedule 2 to the Regulated Activities Order under FSMA 2000. The asset classes that fall within MAR include: (1) transferrable securities, (2) money-market instruments, (3) units in collective investment

undertakings, (3) certain options, futures, swaps and other forms of derivative contracts, (4) emission allowances, amongst others.

⁴ The UK MAR sets out six market abuse behaviours: (1) insider dealing; (2) unlawful disclosure of inside information; (3) manipulating transactions; (4) manipulating devices; (5) dissemination; and (6) misleading behaviour and distortion