

THE OFFENSE OF CAPITAL MARKET MANIPULATION

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Abstract: *The novelty and use of current technology in stock exchange trading operations are just a few reasons for which the capital market domain is a controversial one, and the number of crimes already committed in the financial market raises the issue of securing the supply-demand relationship of capital and capital investment protection. If in the Community law there is no incrimination of market abuse, Romanian legislature sanctioned the capital market manipulation as criminal acts committed intentionally in order to discourage such practices and also to increase the confidence of investors in the financial market.*

Key words: *capital market, handling, dissemination, transaction, regulated market, financial instruments.*

1. Introduction

The normal functioning of a financial markets requires meeting the demand for and supply of financial instruments so that, combined with the large number of capital market operators and market-real transaction price, it would fluctuate naturally and randomly.

From the beginning, we need to specify that the Law no.297/2004 is a special extra criminal law which regulates in matters of the capital market the basic institutions, establishes the main rules and the capital market operations, sets out the rules and obligations of market participants, the administrative authority in the domain of regulation, supervision and control of the capital market, but it also contains rules on the illicit market capital, liability and penalties arising from non-compliance with capital market rules. Regarding the rules on indictment, it must be stated that the legislative technique used in the Law

no.297/2004 is that of referring to other texts of the law.

As an introductory note too, we remind that art.244 of Law no.297/2004 therein includes in its text elements of illicit stock: market abuse and market manipulation capital. There are strong connections between the two legal institutions, in addition to the common body of law text, and therefore in this material we intend to address separately the facts of stock market manipulation, just as the legislature addresses them in art.244 paragraph 5 of Law no.297/2004.

2. Preliminary concepts and definitions

Before analyzing the infringements of the capital market, we will focus on clarifying some common terms that we will use in our approach on the special offense regulated by the Law no.297/2004 - Capital market manipulation.

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According to Article 2 paragraph 1 point 5 in conjunction with article 125 of Law no.297/2004, a *regulated market* is a system for trading financial instruments which: a) operates regularly, b) is characterized by the fact that regulations issued and submitted for approval to National Securities Commission (N.S.C.) define the operating conditions, the market access conditions and the conditions for admission to trading a financial instrument; c) comply with reporting and transparency requirements to ensure investor protection provided by the law as well as the regulations of the National Securities Commission, in accordance with Community legislation. According to Article 126 paragraph 3 of Law no.297/2004 it follows that regulated market is managed by a market operator.

The alternative trading system is the body opposite to the regulated market, as operating under less strict rules, it provides trading securities that do not meet admission requirements on the regulated market (art.139 para.2 of the Law no.297/2004).

While the Romanian legislator defined the regulated market, in case of the capital market we do not have a precise legal definition, so in theory, by interpreting the text of Article 1 paragraph 1 and 2 of the Law no.297/2004, the legal framework and elements of the capital market have been deducted. *De facto*, Cristian Duţescu circumscribes to the notion of capital markets the regulated markets and the multifunctional trading systems^[1]. By reference to capital market elements, Gheorghe Piperea believes that capital market meets three meanings:" (1) the institution organizing the specific transactions to that market; (2) all participants in specific operations and technical systems that made possible carrying out transactions; (3) all transactions generated by the supply and demand of capital investment"^[2].

The same lack of regulatory framework of the Law no.297/2004 is to be encountered too for the transaction, a specific operation of the capital market, omission supplied by internal regulations of the entities involved in the capital market, even if these regulations are inferior in formal terms to the legally binding framework for capital market law. We encounter such definitions in the Central Depository Code, approved by N.S.C. in Decision no.268/22.03.2011^[3], according to which the transaction represents the sale contract concluded in a trading system or outside the regulated market and covers financial instruments admitted into the Central Depository. Similarly, in the presence of the Sibex Depository recognized by the N.S.C. in Decision no.357/31.01.2006^[4], and its acquisition of functions of storage and recording of financial instruments the transaction expanded to the Depository Sibex system too. At position 85 of article 1 paragraph 1 of the Preliminary Title of the Bucharest Stock Exchange Code^[5], the transaction, this time called stock transaction modeled after the Central Depository and Sibex is reported to the financial instruments from the Bucharest Stock Exchange system.

We conclude that irrespective of the trading system, the transaction is the sale and purchase contract which covers financial instruments.

3. The illicit nature of the offense of capital market manipulation

Starting from the everyday definition of the notion of manipulation, where the connotation purely negative, related to fraudulent maneuvers in order to induce false representations of reality and to deceive a subject, the legislature uses the term capital market manipulation, too. There is no doubt that the action aims at deceiving certain persons managing investments or wishing to invest on the

capital market, because manipulation cannot be achieved without casualties. On the other hand, misleading on the price or liquidity of a financial instrument must end with a potential outcome, even if specific investors or capital market participants can't be identified, in order to be in presence of an act of capital market manipulation.

Adding the two afore mentioned aspects, with reference to the provisions of paragraph 5 and 7 from article 244 of Law no.297/2004, we agree with the definition of Cristian Dutescu^[6] according to which capital market manipulation is *the act through which one or more participants in the capital market, have been misled with reference to demand, supply or price of financial instruments, or have been led to conclude transactions at artificial prices or not to sign transactions because of the misleading price due of transactions or transaction orders which have led or kept the price of one or more financial instruments at an artificial level or due to incorrect information provided by the media, internet or other mass media.*

The definition contained in the Romanian doctrine found in article 244 of the Law is in accordance with article 1 paragraph 2 of the European Parliament Directive no.6/2003^[7]. Community and national legal norms similarities are justified by the fact that Romania was in 2004, the year of adoption capital market law, a State on the verge of joining the European Union and therefore was in the process of harmonization of domestic legislation with the communitarian aquis, on the one hand, on the other hand, the lack of local practice under the novelty of the techniques on the capital market, a new field in the post-revolution economy, could prevent the development of a definition or exemption from regulation of practical situations found in the European Directive.

In fact, EU countries have adapted legislation by assimilating the definition in case of manipulation of capital market from the European Directive.

Looking retrospectively at the Romanian legislation in relation to capital market, we find that the first law on securities and stock exchanges^[8] did not define or punish capital market manipulation, there being only certain prohibitions for brokerage houses, with no criminal violations of these prohibitions being penalized.

Government Emergency Ordinance nr.28/2002^[9] introduced for the first time the definition of market manipulation by investors by listing some operations like performing transactions or releasing trading orders which give false or misleading statements about the supply, demand or price of financial instruments, the use of fictitious means for maintaining the price of financial instruments to an artificial level, dissemination of false or misleading information and rumors on demand, supply or price of financial instruments for the same speculative purposes (Article 130 of the G.E.O. no.28/2002) and so, using the same technique as reference in the Law no.297/2004, in paragraph 1 of art. 181 from G.E.O. no. 28/2002 to incriminate the intentional commitment of acts of manipulation described in Article 130.

The market abuse directive establishes an administrative liability (article 14 paragraph 1 Directive no.2003/6/CE), leaving to the national laws the determination of the nature and extent of the sanctions applied by regulating the possibility of accumulation of the administrative responsibility with the criminal liability "*without affecting their right to impose criminal sanctions, Member States make sure that in accordance with national legislation, administrative action may be taken*"^[10].

Corroborating article 279 paragraph 1 with art.248 reported to art.244 paragraph 5 of Law no.297/2004 the offense of capital market manipulation is a crime punishable with imprisonment from 6 months to 5 years or fine and temporary prohibition to conduct activities and services which fall under the Law no.297/2004.

We encounter a similar offense in terms of the objective approach in the Company Law no.31/1990 art.272¹, regulated by adopting Law no.297/2004^[11], and which incriminates the deed of the founder, administrator, manager or company's legal representative, who spreads false news or uses other fraudulent means which have the effect of raising or lowering the value of shares or bonds or other securities the company owns in order to obtain for themselves or for others a benefit to the prejudice of the company.

4. The legal subject and the material object of the offense of capital market manipulation

The offense of capital market manipulation is part of the economic crimes affecting the normal functioning of markets for financial instruments and disturbing mobilization of financial assets, by reference to the provisions of Article 1 paragraph 1 of Law no.297/2004^[12]. The social danger represented by the offense of capital market manipulation is high and therefore required the need to incriminate it as an offense.

The specific legal object of this offense is to protect the activity in the field of capital market against manipulative actions, respectively of the social relations of patrimonial nature acting on the capital market which necessitate a regulated and orderly market, without distortions in its natural mechanism of establishing the trading price for the financial instruments.

Regarding the material object of the offense of capital market manipulation

opinions are divided. Thus, according to Cristian Duşescu^[14], the material object consists in financial instruments admitted to trading on a regulated market. But in this approach, we find that the material object is not direct or tangible, because financial instruments lack materiality given that even their issuing in dematerialized form is a condition for admission to trading on the stock market (article 2 Law no. 297/2004).

We believe that in most ways of the offense referred to in art.244 paragraph 5 of the Law no.297/2004, there is no material element, the only exception being in art.244 paragraph 5 letter c provided by law regarding the dissemination of information in mass media, in which case the material object may be the support, (traditional or electronic), on which the information is printed. Moreover, our conclusion is justified through the fact that if we accepted that the financial instruments constitute the material object of the crime, this would create confusion between the material element and the results obtained by committing the offense.

5. Subjects of the offense

Regarding the active subject, given the wording of the legal text, there are no restrictions justified by the legal nature of the individual, so that both individuals and legal entities can be both active subjects. With reference to the specific legal object, a prerequisite of the quality of active subject is for the legal or natural person to engage in capital market activities, either as an investor or as an intermediary.

If case of a legal person as an active subject, it is stated in the jurisprudence of the High Court of Cassation and Justice^[15] that in addition to sanctioning the legal entity operating on the market of financial instruments guilty of a manipulation offense, the responsibility of individuals who act as administrators, legal representatives or hold managerial

positions in that juridical person can also be committed but it is impossible to punish only the individual in this case, as the one who was culpable of taking action. Regarding the passive subject, we identify the Romanian state as the main subject of interest due to its interest for the capital market to function within normal parameters and specific trading operations to be the result of supply and demand.

At the same time, starting from professor's C.Bulai definition of the passive subject^[16] in the Criminal Law Code (*harmed individual person or legal entity, owner of the social value against whom the offense is directed*) in stock market trading an action of manipulation affects all market participants who show interest in respect of the financial instruments whose price is distorted due to manipulation. Thus, the quality of passive subject of the illegal act of manipulation is common to all those persons of goodwill who participated on the financial instrument market to complete transactions at artificial prices or who could not participate on this market due to maintaining prices at an abnormal level^[17].

6. The material element

To establish the material element of the offense, we resort to the incrimination rule – article 279 paragraph 1 from Law no.297/2004 – incomplete rule reference because after analyzing art.248, to which the rule refers, we must complete the objective content of the offense by analyzing art.244 paragraph 5 of the law where the content of market manipulation is specified.

According to art.244 paragraph 5 of the Law no.297/2004, by transposing into national law the provisions of the Directive against market abuse no.2003/6/CE, capital market manipulation means:

a) transactions or trading orders:

1. *which gives or may give false signals or mislead in relation to the demand,*

supply or price of financial instruments;

2. *which maintain, through the action of one or more persons acting together, the price of one or several financial instruments at an abnormal or artificial level;*

b) transactions or trading orders which employ fictitious devices or any other form of cheating;

c) dissemination of information through mass-media, including Internet or any other way, which gives or may give false signals or misleading information on financial instruments, including the dissemination of rumors and false or misleading news, given that the person who disseminated the information was aware or should have been aware that the information is false or misleading.

Regarding the perpetration of the offense in the manner described in art.244 paragraph 5, letter *a*) of the law, the legislature has placed in the action of manipulation both the conduct of trading execution or trading orders which mislead, as well as operations which give or could give misleading signs the situation when the transactions or trading orders would create a risk of misleading the market participants. In the practice of capital market in Romania, the manipulation through misleading transactions is combined with spreading false information in order to increase the credibility of the action initiated by the manipulator or to create a false impression on the price or liquidity^[18].

In order for the manipulation offense committed under the conditions of article 244 paragraph 5 letter *b* of the law to have an illicit character, it is necessary for the issuing of fictitious trading orders to be followed by actual transactions in favour of the manipulator, although from the legal definition it does not follow, but we otherwise consider that the objective that the manipulator has planned to achieve wouldn't become reality in the absence of transactions.

In the doctrine it was correctly asserted that this form of capital market manipulation (article 244 paragraph 5 letter b of the law) is similar to the qualified version of the offense of fraud incriminated by article 215 paragraph 2 from the Criminal Code.

Current technological developments have had an impact on the way investors influence stock market, as the development of internet and its use on an increasingly larger scale for the transmission of information, including on the capital market, the possibilities to manipulate the market share price have also increased^[19], a reason for which market manipulation through the dissemination of information through the media, including the Internet, has come to be incriminated as a modality of manipulation offense and not as qualified form.

7. Conclusions

Given the structure, organization and principles of functioning of the capital market, the participants on the market, regardless of their structure or financial strength, are motivated in their operations by obtaining a gain from the effective placement of available funds. An important role in the scale and complexity of market operations is played, undoubtedly, by the financial instruments and investor confidence and in obtaining their natural price through the market mechanism of supply and demand. This trust must be maintained and ensured by protecting the investors' interests and providing criminal sanctions for the facts of capital market manipulation.

Thus, the Romanian legislator has opted for criminal liability of participants who use deceptive means and fictitious operations for manipulating the price of the financial instruments and thus of the capital market against the permissiveness of Community rules on market abuse.

Notes

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