

COMMENTS

MARKET MANIPULATION IN RUSSIA AND IN EUROPE: THE CRIMINAL LAW DIMENSION

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DOI: 10.17589/2309-8678-2016-4-3-120-135

This article examines Russian law on criminal market manipulation and compares it with equivalent rules in Western Europe. The Russian rules do not work; no one has been charged or sentenced for market manipulation since the relevant laws came into force. The Russian rules on criminal liability for market manipulation do not complement the general rules on fraud, they duplicate them. Our prohibition on market manipulation is unclear and is not comprehensive, i.e., there are gaps in the law. This prohibition and the criminal law rules based on it require serious revision; it is necessary to eliminate the gaps and make the law clear. It is inappropriate to subordinate the liability for this crime to the fact of causing consequences expressed formally in a sum of money. The rule of law requires a logical generalization. Establishing criminal liability for negligent market manipulation in Russia seems premature.

Keywords: market manipulation; criminal liability; Market Abuse Directive 2014 (MAD); Market Abuse Regulation 2014 (MAR); Article 185³ of the RF CC Code; gaps in the law.

Recommended citation: Ivan Klepitskij, *Market Manipulation in Russia and in Europe: the Criminal Law Dimension*, 4(3) Russian Law Journal 120-135 (2016).

1. Introduction

On 3 July 2016 the EU Market Abuse Regulation (the MAR)¹ came into force. As a result, basic definitions of illegal market manipulation in the national laws of the

¹ Regulation (EU) No. 596/2014 of the European Parliament and of Council of 16 April 2014 on Market Abuse (Market Abuse Regulation) and Repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC.

EU Member States are gradually losing their effect. German lawmakers, for example, simply erased them, directly referring to the MAR.² Now, Art. 12–15 MAR provides the definition of illegal market manipulation, having direct effect. The Market Abuse Directive (MAD) also limits national legislators regarding criminal sanctions.³

The MAR builds upon a century of European and American experience of combating market manipulation, including the Dodd-Frank Wall Street Reform and Consumer Protection Act⁴ and extensive jurisprudence. The MAR deserves close study as culturally valuable not only in the EU, but also in Russia. Modern markets of securities and various derivatives are global and they do not know national boundaries. In addition, it is necessary to take into account the fact that the MAR prohibitions apply to acts or omissions committed outside the territory of the EU.

The Russian Federal law of 30 October 2009 added Art. 185³ (On the Manipulation of Prices in the Securities Market) to the Russian Federation Criminal Code (Ugolovnyj kodeks Rossijskoj Federacii, RF CC), it was the first legal counteraction of market manipulation in Russia. The Federal Law On the Prevention of Unlawful Use of Insider Information and Market Manipulation and On Amendments to Certain Legislative Acts of the Russian Federation of 27 July 2010 presented this article in a new edition titled Market Manipulation.⁵ Since 2009, no one has been charged or sentenced under Art. 185³ of the RF CC. There are, however, a few administrative decisions related to the facts of market manipulation⁶ (e.g., broker and other license cancellations, and administrative fines).⁷ In 2010, Russia had no significant experience of such

² Erstes Gesetz zur Novellierung von Finanzmarktvorschriften auf Grund europäischer Rechtsakte (Erstes Finanzmarktneuordnungsgesetz – 1. FiMaNoG) vom 30.06.2016. BGBl. I S. 1514 [First Law Amending Financial Market Regulations under European Legislation (First Financial Markets Act Amendment – 1. FiMaNoG) of 30 June 2016].

³ Directive 2014/57/EU of the European Parliament and of the Council of 16 April 2014 On Criminal Sanctions for Market Abuse (Market Abuse Directive).

⁴ Public Law 111-203 21 July 2010.

⁵ Собрание законодательства Российской Федерации [Sobranie zakonodatel'stva Rossiiskoi Federatsii [Russian Federation Collection of Legislation]] 2010, No. 31, Item 4193. There is an opinion that “in the field of securities market regulation Russia basically implemented EU Directive 2003/6/EC of 28 January 2003 on insider dealing and market manipulation (market abuse), and the rules adopted by the European Commission pursuant to this Directive, as well as the experience of its implementation in Germany and the United Kingdom” (Paul Kalinichenko, *Practice of Legislative Approximation in Russia. Legislative Approximation and Application of EU Law in the Eastern Neighborhood of the European Union: Towards a Common Regulatory Space?* 254 (Ed. by Peter Van Elsuwege & Roman Petrov, Routledge 2014)). A detailed investigation of the rules of law does not allow us to agree with this opinion.

⁶ See: Identified cases of unauthorized use of insider information and market manipulation, available at <http://www.cbr.ru/finmarkets/?PrtlId=inside_detect> (accessed July 8, 2015).

⁷ Art. 15.10 of the Code of Administrative Offences provides for market manipulation fines for individuals of up to 50 thousand rubles (less than US \$ 1,000) or disqualification for up to two years. A corporation can be fined in the amount of the benefits received from the manipulation.

legislation and Russian stock exchanges were rudimentary and weighed down with bureaucratic measures. The situation has not changed for the better.⁸

In such circumstances, the study of the European experience and a comparison of Russian rules on market manipulation with Western European rules may be appropriate and useful.

2. Market Manipulation under EU Rules

The MAR Prohibition on manipulation applies to *regulated markets, and multilateral and organized trading facilities* (MTF and OTF) for (a) *financial instruments* (transferable securities, money-market instruments, units in collective investment undertakings, derivative contracts relating to financial instruments as well as to commodities, derivative contracts relating to commodities etc.); (b) *spot commodity contracts*; and (c) *auctioned products based on greenhouse gas emission allowances*.

Rule 10b-5, issued by the U.S. Securities and Exchange Commission (SEC rule 10b-5),⁹ provides protection against manipulation not only for regulated markets but also for 'any means or instrumentality' of commerce. The MAR not only protects regulated markets, MTF and OTF against manipulation (Art. 2 § 1) but also any spot commodity contract markets and any markets of all types of financial instruments and applies to behavior in relation to benchmarks (Art. 2 § 2–4), prohibiting related actions and omissions in the EU and other countries.

The MAR covers practically all types of derivatives, regardless of their base.

MAR Art. 12 § 1(a) defines market manipulation in relation to these objects as *transactions, placing orders or any other behavior* which:

- 1) "gives, or is likely to give, *false or misleading signals* as to the demand for, or supply or price of" these objects; or
- 2) "secures, or is likely to secure, *the price*" of these objects "*at an abnormal or artificial level*".

⁸ The level of stock market development in Russia and the quality of its legal regulation can be illustrated by a curious example. The Federal Law of 27 July 2010 provided for the duty to draw up comprehensive 'lists of insider information' and publish insider information in the prescribed order. The Federal Law of 21 July 2014 stated that those obligations do not apply to issuers of foreign securities if the securities are admitted to organized trading without a contract between the organizer of trade and the issuer. Other issuers continue to bear this burden. Russian issuers are now required to disclose the information twice: 1) as the issuers in accordance with the law on the securities market; and 2) as those who disclose information in accordance with the law on market abuse. Facts such as 'the factory burned down', 'the director committed suicide' etc. are not regarded as insider information in this regulation. Russian society and authorities are not aware of the value of the financial market and the stock exchange; they only tolerate them as a dangerous coven of speculators who are not related to the 'real economy'. Legislation on financial markets in Russia is developed under the influence of international organizations which Russia aspires to join. See for example: OECD Reviews of Regulatory Reform. Russia. Building Rules for the Market 72 (2005), available at < <http://www.oecd.org/russia/russiabuildingrulesforthemarket-oecdreviewsoregulatoryreform.htm>>.

⁹ US Code of Federal Regulations, § 240.10b-5.

The combination of these two acts is not required, either one of them is sufficient. Therefore, both causing effects (securing price), and, defined very broadly, acting to cause effects (giving signals)¹⁰ are punishable. The signals must be false or misleading. The prices must be abnormal or artificial. However, there does not need to be an intention to defraud, nor intent to take advantage for oneself or another, nor evidence of having taken advantage of losses caused. Market manipulation is not fraud. The prohibition on market manipulation is particularly useful when it is difficult to prove fraud.

A non-exhaustive list of indicators of manipulative behavior relating to 'false or misleading signals' and 'price securing' is set out in MAR Annex I: a) the extent to which orders and sales represent a significant proportion of the volume of transactions, in particular when those activities lead to a significant change in their prices; b) the extent to which orders or sales by persons with a significant buying or selling position in a financial instrument lead to significant changes in the price of that financial instrument; c) whether transactions lead to no change in beneficial ownership; d) the extent to which orders or sales include position reversals in a short period and represent a significant proportion of the daily volume of transactions and might be associated with significant changes in the price of a financial instrument; e) the extent to which orders or sales are concentrated within a short time span in the trading session and lead to a price change which is subsequently reversed; f) the extent to which orders given change the representation of the best bid or offer prices, or, more generally, the representation of the order book available to market participants, and are removed before they are executed; and g) the extent to which orders or transactions are undertaken at or around a specific time when reference prices, settlement prices and valuations are calculated and lead to price changes.

Exceptions to the prohibition are made for cases when the act is committed 'for legitimate reasons', and 'conform[s] with an accepted market practice.' These exceptions are specified in Art. 13 (accepted market practices). A competent authority (designated by a Member State), may, after notifying the European Securities and Markets Authority (ESMA) and other competent authorities (designated by other States), consider the practice is acceptable (seven reasons are listed in Art. 13 § 2 'a–g'). Additional exceptions are made for buy-back programs, for trading in securities or associated instruments for the stabilization (Art. 5) and for monetary and public debt management and climate policy activities (Art. 6).

¹⁰ In Germany, for example, the prohibition on 'signals' per se means expanding the range of criminal offenses, when committed intentionally. See *Das künftige Kapitalmarktstrafrecht – verschärfte Regelungen und Verfolgungsmöglichkeiten* [The future German Capital Markets Criminal Law – tightened regulations and prosecution options], Clifford Chance Newsletter, 25 May 2016, at 3, available at <https://www.cliffordchance.com/briefings/2016/05/das_kuenftige_kapitalmarktstrafrechtverschaeerft.html> (accessed July 12, 2016). In the UK, the expansion of the definition of punishable behavior does not occur due to the Financial Services Act 2012 sec. 90, which prohibits 'any act' or engagement "in any course of conduct which creates a false or misleading impression as to the market in or the price or value of any relevant investments."

MAR Art. 12 § 1 'b-d') defines three distinct forms of market manipulation and these forms are not covered by the exceptions in Art. 13.

§ 1(b) prohibits any "activity or behavior which affects or is likely to affect the price" which employs a "fictitious device or any other form of deception or contrivance."¹¹ A non-exhaustive list of indicators of "employment of a fictitious device or any other form of deception or contrivance" is set out in MAR Annex I: a) orders or sales by persons are preceded or followed by dissemination of false or misleading information by the same persons or by persons linked to them; and b) orders or sales by persons before or after the same persons or persons linked to them produce or disseminate investment recommendations which are erroneous, biased, or demonstrably influenced by material interest.

§ 1(c) prohibits *disseminating information*, which a) *gives, or is likely to give, false or misleading signals* as to the supply, demand or price; or b) *secures, or is likely to secure, the price at an abnormal or artificial level.*¹² 'Information' is understood broadly, including rumors. *Recklessness* is punishable if the person knew, or ought to have known, that the information was false or misleading.

§ 1(d) prohibits any behavior, which manipulates the *calculation of a benchmark*, "any rate, index or figure, made available to the public or published that is periodically or regularly determined by the application of a formula to, or on the basis of the value of one or more underlying assets or prices, including estimated prices, actual or estimated interest rates or other values, or surveys, and by reference to which the amount payable under a financial instrument or the value of a financial instrument is determined" – Art. 3 § 1(29).

MAR Art. 12 § 2 gives examples of conduct which are considered market manipulation, *inter alia*:

a) the conduct by a person or a pool to secure a dominant position over the supply or demand, "which has, or is likely to have, the effect of fixing, directly or indirectly, purchase or sale prices or creates, or is likely to create, other unfair trading conditions";

b) "marking the closing or opening market", "which has or is likely to have the effect of misleading investors acting on the basis of the prices displayed";

c) placing, cancelling or modifying orders by any means, including algorithmic, if it has one of the effects referred to in Art. 12 § 1(a) or (b) by (1) "disrupting or delaying the functioning of the trading system... or being likely to do so;" (2) "making it more difficult

¹¹ Compare with the US SEC rule 10b-5: "It shall be unlawful for any person, directly or indirectly, ... (a) To employ any device, scheme, or artifice to defraud ..., 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...."

¹² Compare with the US SEC rule 10b-5: "It shall be unlawful for any person, directly or indirectly, ... (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 ..." In the case of 'information manipulation' (in the US or Europe) the consequences are not required. The omission falls under MAR Art. 12 § 1(a).

for other persons to identify genuine orders...,” (3) “creating or being likely to create a false or misleading signal about the supply of, or demand for, or price of, a financial instrument, in particular by entering orders to initiate or exacerbate a trend¹³,”

4) the taking advantage of access to the media by voicing an opinion and profiting subsequently from the impact of the opinions without having simultaneously disclosed the relevant conflict of interest to the public;

5) the buying or selling on the secondary market of greenhouse gas emission allowances or related derivatives prior to an auction.

MAR Art. 15 prohibits any person “to engage in or attempt to engage in market manipulation”, referring to the definition of prohibited conduct in Art. 12. MAR Art. 30 provides an extensive list of administrative sanctions: order to cease the conduct; disgorgement of the profits gained or losses avoided; public warning; withdrawal or suspension of the authorization of an investment firm; a temporary ban on exercising management functions in investment firms; and pecuniary sanctions. Pecuniary sanctions for market manipulation in respect of an individual must be at least 5 million euros, and, in respect of a corporation, 15 million euros or 15% of the total annual turnover.

The criminal penalties for market manipulation with regard to the provisions of the MAD are introduced by national legislators. MAD Art. 7 stipulates that the maximum criminal penalty for market manipulation (“in serious cases and when committed intentionally”) should be imprisonment of at least four years.

These requirements are implemented¹⁴ by national legislatures. For example, the German Securities Trading Act (as amended by the Law of 30 June 2016) establishes sanctions for manipulation in respect of an individual: a pecuniary sanction of up to 5 million euros for violation of MAR Art. 15 (§ 39) and, if committed intentionally,

¹³ In the age of electronic trading, the danger of such abuse is high. They considered one of the causes of the ‘Flash Crash’ on May 6, 2010 that resulted in the Dow Jones Industrial Average falling by 9 percent for a short period. According to information from the US authorities, London trader Navinder Singh Sarao made 878 thousand US dollars just on this day by spoofing etc. The trade was algorithmic. Within 12 minutes, he placed 135 orders for sale, and then canceled 132 of them. In 2015, the US Department of Justice asked the British authorities to extradite Sarao for prosecution on 22 criminal counts, including fraud and market manipulation. His defense insisted on that the act is not punishable under English law. However, in March 2016, Westminster Magistrates’ Court rejected the arguments of the defense and, in May, the Home Office decided to extradite him.

¹⁴ There are problems with the implementation, e.g., in Spain. Spanish Penal Code Art. 284 does not comply with the MAD definition of offenses or the sanctions it provides. See Gómez-Benítez, José Manuel, Aspectos penales fundamentales de la reciente Directiva y del Reglamento sobre abuso de mercado [The main criminal law aspects of the recent Directive and the Regulation on market abuse], *Análisis GA&P*. Junio 2014. In Italy and France the implementation was complicated with the European Court of Human Rights’ judgment in the case of Grande Stevens and Others v. Italy. The Court found the administrative sanctions were criminal and stated the fact of violation of the principle *ne bis in idem*. See Dan Benguigui, *The French legal regime on market abuse: what next?* *Eur. Fin. Litigation Rev.*, 2015, November, available at <<http://www.allenoverly.com/publications/en-gb/european-finance-litigation-review/western-europe/Pages/The-French-legal-regime-on-market-abuse-what-next.aspx>> (accessed July 12, 2016).

criminal penalties of up to 5 years imprisonment or a fine (§ 38). An attempt is punishable. In particularly serious cases,¹⁵ imprisonment can be imposed for up to ten years. The French Monetary and Financial Code Art. L465-1 also provides for imprisonment up to 5 years. The Italian Legislative Decree of 24 February 1998 Art. 185 provides for up to 6 years. The UK Financial Services Act 2012 Sec. 92 provides for up to 7 years. The Czech Penal Code § 250 provides for up to 10 years.

Mens rea for market manipulation is subject to national law. Consider, for example, the German rules. Article § 39-3d-2 of the Securities Trading Act provides that: "Someone who violates Regulation (EU) No. 596/2014 by knowingly or recklessly ... committing a market manipulation contrary to Article 15 commits an administrative offense." According to § 38-1-2: "imprisonment up to five years or a fine will be imposed on anyone referred to in Article ... § 39-3d-2 who commits knowingly and thus affects ... prices... or ... benchmarks." Criminal market manipulation in Germany can be committed with both *dolus directus* and *eventualis*.¹⁶

In the UK, the law is more severe, Part 7 of Financial Services Act 2012 provides a criminal penalty both for willful and for reckless market manipulation. This applies both to 'misleading statements' (sec. 89) and to 'misleading impressions' (sec. 90): "a person knows that the impression is false or misleading or is reckless as to whether it is."

Therefore, the legal prohibition of market manipulation in Europe is defined very broadly, it refers to both the *actus reus*, and to *mens rea*. Let us compare it with the widest definition given under the US SEC rule 10b-5 (c): "To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person." Intent is not required for the prosecution of this offense, but the rule created by the US Supreme Court in *Ernst & Ernst v. Hochfelder*¹⁷ that *negligence* does not give rise to liability (criminal or civil) remains in force. This rule has only been partly overcome through legislation¹⁸ regarding information-based manipulation schemes. The Securities Exchange Act of 1934, § 9(a)(4) prohibits brokers, dealers, others offering or selling security from making statements they know and *should know*

¹⁵ For those who acted as professional criminals or as members of a gang or acted, in the course of their work for a financial supervisory authority, a security services company, an exchange or an operator of a trading venue.

¹⁶ *Dolus eventualis* in German and Russian law is not recklessness, but 'knowledge' without intent. Recklessness (*Leichtfertigkeit*) in § 39-3d-2 Securities Trading Act is not *dolus*. See Das künftige Kapitalmarktstrafrecht – verschärfte Regelungen und Verfolgungsmöglichkeiten, Clifford Chance Newsletter, 25 May 2016, at 2, available at <https://www.cliffordchance.com/briefings/2016/05/das_kuenftige_kapitalmarktstrafrechtverschaeft.html> (accessed July 12, 2016). Russian lawyers also distinguish between a real and an abstract threat of harm. When the offender acts knowing the real threat of harm and allows such harm to occur or is indifferent to the harm, it is *dolus eventualis*. When the offender acts knowing of the abstract possibility of harm (that can arise in such situations), but hopes that, in this particular case, harm will not come to pass, it is not *dolus*.

¹⁷ See *Ernst & Ernst v. Hochfelder*, 425 U.S. (1976).

¹⁸ Dodd-Frank Wall Street Reform and Consumer Protection Act 2010.

to be false or misleading for the purpose of inducing purchase or sale of securities.¹⁹ To this day, there is no legal certainty as regards the ‘open-market manipulation’ theory,²⁰ different federal courts of the same level issue different decisions in similar situations.²¹ Although the definitions of the American rule are not as wide as the European, this rule can also be used when evidence for fraud is not sufficient.

Global trends in this area are:

- 1) a broad understanding of prohibited market manipulation (including negligence);
- 2) strengthening penalties for it; and
- 3) a dangerous expansion of discretionary powers of the administrative authorities.

3. Market Manipulation under Russian Law

The prohibition on manipulation in the Russian Federal Law of 27 July 2010 applies only to ‘organized trading’ (Art. 1). ‘Organized trading’ is defined as “trades conducted on a regular basis according to established rules” which “provide for the procedure for the admission of persons to participate in trading for the conclusion of contracts of sale of commodities, securities, foreign exchange, repo contracts and contracts which are derivative financial instruments.”²² A trades organizer can be ‘stock exchanges’ or ‘trading systems’ licensed by the Bank of Russia.

Russian law, in contrast to European and US law, does not prohibit market manipulation outside ‘organized trading’.

The objects of organized trades and market manipulation may be:

- a) financial instruments, foreign currency or commodities admitted to organized trading on the territory of the Russian Federation;
- b) those of the above for which an application for admission to organized trading has been made; or
- c) financial instruments whose price depends on the price of a) or b) above.

‘Financial instruments’ are securities and derivative financial instruments.²³ ‘Securities’, which are considered financial instruments, include the following according to Federal Laws: stocks, employee stock options, bills of exchange and promissory notes, mortgages, mortgage-backed securities, investment shares of a mutual investment fund, bills of lading, anonymous passbooks, certificates of

¹⁹ Compare with MAR Art. 12 § 1(c). European rules do not only apply to persons offering or selling security.

²⁰ See Maxwell K. Multer, *Open-Market Manipulation under SEC Rule 10b-5 and its Analogues: Inappropriate Distinctions, Judicial Disagreement and Case Study: FERC’s Anti-Manipulation Rule*, 2 Sec. Reg. L. J. P. 97 ff. (2011).

²¹ See Mitchell E. Herr, *Koch v. S.E.C. (D.C. Cir. July 2015): The First Article III Endorsement of the SEC’s Marking the Close Theory*, Sec. Reg. & L. Rep., 47 2083, 11/2/15.

²² Federal Law of 21 November 2011 on Organized Trading, Art. 2.

²³ Federal Law of 22 April 1996 on the Securities Market, Art. 2.

deposit, bonds, checks, clearing certificates of participation and warehouse receipts. 'A derivative financial instrument' is defined in law as a "contract, providing for one or more of the following duties..." What follows is a casuistry list of possible duties. Repurchase agreements shall not be considered derivatives.

A literal interpretation of the law would lead to the conclusion that market manipulation of derivatives or Russian rubles is not prohibited since it is not covered by Russian law. Russian law has no effect on market manipulation abroad, even if Russian investors are damaged. But it should be borne in mind that a broad interpretation of the law is not excluded if the need arises.

According to the Bank of Russia²⁴ from 25 March 2010 to 8 July 2016 a total of 54 cases of market manipulation and only 2 cases of insider abuses were revealed. The objects of manipulation were stocks, investment shares and bonds. Manipulation with respect to other financial instruments was not revealed.

Prohibitions on market manipulation given in Art. 185³ of the RF CC and in the Federal Law of 27 July 2010 On the Prevention of Unlawful use of Insider Information and Market Manipulation... Art. 5 contradict each other.

Art. 5 prohibits manipulation in 7 forms: 1) dissemination of false information; 2) making operations by prior agreement; 3) making transactions for the account or benefit of one person; 4) counter orders; 5) making transactions for the account or benefit of one person at the highest purchase price or lowest selling price, repeated in one trading day; 6) commission for the account or benefit of one individual transaction in order to mislead on the price, repeated during one trading day; 7) a repeated failure to fulfill obligations under the transactions made without the intention to execute the same, with the same financial instrument, foreign currency or commodity.

The legislative technique in Art. 5 is not perfect, it is difficult to understand and inaccurate in terms of legal certainty.

All seven forms of manipulation are prohibited if they result in:

a) "the price, demand, supply and trading volume... deviating from the level or maintained at a level significantly different from the level which would have formed without" such behavior (for forms 1–4, 7):

b) "the price... significantly deviating from the level that would have formed without such transactions" (for form 5); and

c) "the price... being maintained at a level significantly different from the level which it would have been without such transactions" (for form 6).

The criteria for 'substantial deviation' should be established by the trade organizer (stock exchanges and trading systems) based on the *guidelines* of the Bank of Russia. Until 2013, the Federal Financial Markets Service (FFMS) drew up these guidelines. Trade organizers prefer not to establish such criteria and refer to guidelines given

²⁴ The list of detected cases of illegal use of insider information and market manipulation can be found at <http://www.cbr.ru/finmarkets/?Prtd=inside_detect> (accessed July 8, 2015).

by the FFMS and the Bank of Russia²⁵. The FFMS-approved guidelines' compliance with the law is questionable. Given the fact that these guidelines are supposed to distinguish between lawful behavior and crimes they are unsatisfactory. The law requires a causal link between manipulative acts and a "significant deviation". The guidelines ignore causality. The guidelines offer simple mathematical formulae not to characterize the results of concrete conduct but to describe the state of a market without making any connection with this conduct and without taking into account the various factors of the market.

This is most obvious with regard to the foreign exchange market. In 2012, the FFMS recommended considering transactions (orders) with a significant price deviation as "transactions (orders), having the characteristics of market manipulation." The FFMS recommended to setting 'price bands' for orders to buy and to sell currencies and based on currency swaps, and stated that: "It is recommended to recognize transactions as having a significant deviation in the price, if, in the course of trading, ...: (1) the prices of the transactions ... were at a price band boundary ... which led to the need to adjust it; (2) the prices of orders ..., on the basis of which transactions were made, were at a price band boundary ... which led to the need to adjust it; (3) the price of swaps were at a price band boundary ... which led to the need to adjust it; (4) the prices of orders to enter into swaps with the direction of the 'sale / purchase' or 'buy / sell', on the basis of which swap a transaction was made, were at ... band boundary ... which led to the need to adjust it."²⁶

The Bank of Russia went further, approving the 23 March 2016 Guidelines for the Establishment of Criteria for a Significant Deviation of Price, Demand, Supply, and Trading Volume of Illiquid Securities,²⁷ giving rise to legal uncertainty and the risks arising from it. The Bank recommended that exchanges set their own criteria (without any recommendations) and inform Expert Council on Significant Market Deviations about these criteria. In addition, it is recommended to contact the Expert Council to determine whether the transactions (orders) resulted in significant deviation, the question will be considered after the fact, absent a clear indication.

Forms of market manipulation defined in the law are long-winded and unjustifiably difficult.

The *first form* of manipulation (dissemination of false information) is prohibited if person acted knowing the information is false and intended to manipulate the price, etc. Recklessness and *dolus eventualis* is not punishable.

All other forms include operations, transactions or placing orders to buy or sell. Article 2 defines 'operations' as "transactions and other acts aimed at the purchase

²⁵ See Moscow Exchange. Data for defining criteria of significant deviations, available at <<http://moex.com/a777>> (accessed July 12, 2016).

²⁶ Guidelines for the establishment of criteria for a significant price deviation for foreign currency, approved by Order of the FFMS of 12 July 2012.

²⁷ Bulletin of the Bank of Russia, 2016, March 30, No. 33.

or sale ... , as well as acts obliging the performance of such acts, including placing orders to buy or sell."

The *second form* (probably meaning the pool) requires "preliminary agreement between traders and/or their employees and/or persons for the account or benefit of which these operations are carried out." The word 'agreement' in Russian means any expression of the concerted will of two or more persons. The term 'preliminary' in criminal law applies to conspiracy to commit a crime and indicates that the conspiracy took place before committing the act constituting the *actus reus* of the crime.

Possible interpretations of the term 'preliminary agreement' are: a) an agreement entered into before 'making operations'; and b) an agreement entered into before the prohibited manipulation. The first variant does not make clear the cause for agreement. If, for example, a trader agrees with the broker on the margin, it is clear that this agreement is not relevant. Therefore, the second variant seems to be the proper interpretation, and it suggests the intention to manipulate the market, which is the cause for the agreement. In fact, the substantial condition of a pool is the distribution of profits and losses between traders. However, the law does not disclose the essence of prohibited agreement, so the law is not clear. Arbitrary interpretations are possible, any operation can be declared manipulation in this form if unfair or tendentious interpretation of the law will happen.

The *third form* of manipulation involves transactions and obligations a) for the account of one person; b) for the benefit of one person. This person is probably a final beneficiary, controlling formally independent traders (as opposed to the pool presented in the second form.) This interpretation also requires the intention to manipulate the market.

The *fourth form* involves placing orders to buy or sell for the account or benefit of one person, if the result of which is that "at the same time, two or more opposite orders appear in which the purchase price is higher than or equal to the selling price of the same, if transactions are made on the basis of these orders." We can assume this is spoofing'. However, the law clearly states that the influence on the market should not be the result of placing orders, it should be the result of transactions on the basis of these orders. The situation regarding the cancellation of orders is not considered at all, including high-frequency and algorithmic trade.

The *fifth form* is "repeated throughout the trading day making March ... transactions for the account or benefit of one person on the basis of orders, having, at the time of placing, the highest purchase price or the lowest selling price, if the result is that the price is significantly deviated from the level, which would have formed without such transactions. For this form is necessary the intention to making of opposite transactions (by or for the benefit of the same or another person) by artificial prices. Subsequent commission of such opposite transactions is the separate mode of this form of manipulation.

For the *sixth form* of manipulation is also necessary intention to manipulate, with the goal being to mislead regarding the price. The act is defined widely as

a) “commission for the account or benefit of one person transactions, repeated in one trading day.” A single transaction (‘marking the close’) cannot be declared manipulation in this form. b) “price... was significantly deviated from the level that would have formed without such transactions” (for form 5), c) “price... was maintained at a level significantly different from the level which would have formed without such transactions” (for form 6). The consequence of this act must be the ‘maintenance’ of price, ‘deviation’ is not relevant.

Lastly, *the seventh form* of manipulation is difficult to understand. The law prohibits “repeated failure to execute obligations under the operations made without the intention of their execution, with the same financial instrument” etc. Apparently, the law does not prohibit the placing and cancellation of orders for manipulating the market. A canceled order does not lead to the entry into an obligation.

Forms of manipulation 2–4 are only prohibited for *anonymous trading*, if “transactions made on the basis of orders addressed to all traders, in case the information on the persons who issued these orders, as well as on the persons for the benefit whom issued these orders, are not disclosed to other traders. Forms 5–7 are prohibited for any organized trading.

Federal Law of 27 July 2010 Art. 5 is an example of legal technique error. When a particular case is elevated to a general rule without the necessary generalization, gaps in the law as a result are inevitable. So none of the prohibited forms of manipulation cover the ‘spoofing’. In general, the legislative technique in Art. 5 is not perfect, it is difficult to understanding and inaccurate in terms of legal certainty. The situation with the criminal law rule on market manipulation is similar. The problem is probably that “most provisions of the ‘insider information law’ have been ideally drafted by securities market experts”²⁸, legal experts did not work enough with these ‘statements’.

The authors of the commentary to the Federal Law of 27 July 2010 pointed out: “... The authors of many laws often do not attach proper attention to purposes of future laws and formulate them without a thorough understanding of what, in my opinion, happened in the case of the commented Law.”²⁹ This view seems correct.

²⁸ Анищенко Е.В. *Проблемы противодействия применению инсайдерской информации и манипулированию рынком ценных бумаг в России*, 2 Конкурентное право 23 (2014) [Anishchenko E.V. *Problemy protivodeystviya primeneniyu insayderskoy informatsii i manipulirovaniyu rynkom tsennykh bumag v Rossii*, 2 Konkurentnoe pravo 23 (2014) [Evgeniy V. Anishchenko, *Problems of Counteraction of Use of Insider Information and Market Manipulation of Securities in Russia*, 2 Competition L. 23 (2014)]].

²⁹ Емельянов А.С., Федотов В.Н., Вавулин Д.А. *Комментарий к Федеральному закону «О противодействии неправомерному использованию инсайдерской информации и манипулированию рынком и о внесении изменений в отдельные законодательные акты Российской Федерации» 7 (Москва 2011)* [Emel'yanov A.S., Fedotov V.N., Vavulin D.A. *Kommentariy k Federal'nomu zakonu "O protivodeystvii nepravomernomu ispol'zovaniyu insayderskoy informatsii i manipulirovaniyu rynkom i o vnesenii izmeneniy v otdel'nye zakonodatel'nye akty Rossiyskoy Federatsii" 7 (Moscow 2011)* [Aleksandr S. Emel'yanov, Vyacheslav N. Fedotov, Denis A. Vavulin, *Commentary to the Federal Law On the Prevention of the Unlawful Use of Insider Information and Market Manipulation and On Amendments to Certain Legislative Acts of the Russian Federation 7 (Moscow 2011)*]].

Art. 185³ of the RF CC provides criminal punishment (up to four years imprisonment) for three criminal forms of market manipulation, if such manipulation results in deviation or maintaining an artificial price, demand, offer or volume of trading and thereby causes: a) large-scale losses; b) large-scale surplus income; c) avoidance of losses on a large scale. Imprisonment may be imposed for up to seven years if the act is committed by an organized group or on an extremely large scale.

'Large-scale' means more than 2.5 million rubles, 'extremely large-scale' means more than 10 million. 'Surplus income' is "the difference between the income obtained as a result of illegal actions and the income that would have been obtained without the illegal actions."

Describing the features of the crime, it should be noted that the law has not been tested in practice, i.e., no one has been charged under this article.

The criminal forms of market manipulation are: 1) intentional dissemination of knowingly false information; 2) operations with financial instruments, foreign currency or commodities; 3) other intentional acts prohibited by the legislation of the Russian Federation on combating ... market manipulation.

Analysis of the text of the law leads us to the conclusion that the three forms of criminal manipulation require 'double illegality', i.e., the act being prohibited both in the Federal Law of 27 July 2010 Art. 5 and in Art. 185³ of the RF CC. This conclusion is indirectly indicated by the words "or any other intentional acts prohibited by the legislation of the Russian Federation on combating ... market manipulation". The word 'other' indicates forms 1 and 2 of criminal manipulation should also be "intentional acts prohibited by the legislation of the Russian Federation on combating ... market manipulation." This allows us to generalize the rule, the forms 1 and 2 of criminal manipulation having lost their separate legal value.

Let us continue with the generalization. The law indicates the results of manipulation: the property losses and the property gains (surplus income and avoidance of losses). Speculation on financial markets does not result in real value or benefit for one person corresponding to the losses of another, and *vice versa*. Intentional behavior of a sane person is always directed to the achieving his own interests (property and other, e.g., vengeance and altruism). The study of the seven forms of manipulation prohibited by the Federal Law of 27 July 2010 Art. 5 shows that all these forms are associated with the intent to defraud (in the broadest sense of the word, in which not only a human can be deceived, but also a robot involved in algorithmic trading). The results of generalization are: 1) personal interest leads to the concrete goals (causing property benefits for yourself or another, causing harm to another etc.) and 2) the intention to defraud in order to achieve these goals through deception.

It is important that the generally accepted technique in Russia of interpretation of the RF CC leads to the understanding of intention under this rule as relating both to the manipulation, and to its results (losses and benefits).

Therefore, Russian criminal market manipulation meets all the criteria for fraud (Art. 159 and 159⁶ of the RF CC), both *actus reus* and *mens rea*. Our criminal market manipulation is beyond the scope of fraud only in two cases:

1) when it was committed without the aim of gaining property benefits (of vengeance, for example);³⁰ and

2) when the damages are not a loss of money or other property, but something else (loss of profits, consequential loss).

In such circumstances, it is important to understand the mutual relationship of rules on market manipulation and fraud.

Market manipulation does not lead to criminal liability if its size is not 'large-scale' (more than 2.5 million rubles). Fraud is a criminal offence if the benefits gained therefrom exceed one thousand rubles. Fraud with benefits exceeding one million (Part 4 Art. 159 of the RF CC) is punishable by imprisonment of up to 10 years. The most severe penalties for market manipulation is imprisonment of up to seven years.

Market manipulation with all the attributes of fraud cannot be regarded as a less serious crime than fraud; it not only causes damage to property, but also destroys public confidence in the investment market. Therefore, the rule on market manipulation is to apply when there are no attributes of fraud at all.

The definition of results in the form of a sum of money is another reason that the criminal law rule on market manipulation does not work.³¹ We have seen that there is no satisfactory method of accurately calculating the 'significant deviation'. It is more difficult to develop a credible method for calculation of losses and benefits suitable for a criminal charge.

4. Conclusion

The Russian financial market is underdeveloped, and this hinders the development of the economy as a whole. This market requires gentle handling. The first experience in legal prevention of market manipulation was not very successful. Nevertheless, we are enriched by this experience. It is time to correct mistakes. Currently, Russian rules on market manipulation duplicate rules on fraud rather than complement them. It is considered that, for this crime, the intent to cause loss of benefit is required;

³⁰ Art. 165 UK RF covers this case. UK Fraud Act 2006 Art. 2 also partially covers this case, defining it as a kind of intention "to cause loss to another or to expose another to a risk of loss."

³¹ See Флерова У.А. Особенности доказывания манипулирования рынком по уголовным и административным делам, 5 Адвокат (2012) [Flerova U.A. *Osobennosti dokazyvaniya manipulirovaniya rynkom po ugovolnym i administrativnym delam*, 5 Advokat (2012) [Uliana A. Flerova, *Characteristics of Evidence for Market Manipulation in Criminal and Administrative Cases*, 5 Advocate (2012)]. See also Долотов Р.О. Проблемы привлечения лиц к уголовной ответственности за манипулирование рынком, 3 Адвокат (2016) [Dolotov R.O. *Problemy privlecheniya lits k ugovolnoy otvetstvennosti za manipulirovaniye rynkom*, 3 Advokat (2016) [Ruslan O. Dolotov, *Problems of Criminal Prosecution for Market Manipulation*, Advocate 3 (2016)].

the intent to manipulate markets is not enough for prosecution. *Dolus eventualis*, recklessness and negligence are not punishable. The rule is not generalized, *actus reus* is presented in an unnecessarily complicated list of acts which is not exhaustive. However, the main problem today is not gaps in the law, but legal uncertainty, born from the obscurity of the law. This legal uncertainty deters investors from trading in the market. In such circumstances, it is desirable to make the law clear and accurate so that it is useful for people trading on exchanges.

It is advisable to improve Russian rules on punishable market manipulation. 'Details' are important. Manipulation should lead to liability regardless of the size of losses or benefits. Losses and benefits should be excluded from evidence of a crime. However, the intention to gain an advantage for oneself or another person as a result of market manipulation may be provided as an element of a crime. Criminal liability for negligence is unreasonable in relation to market manipulation. In order to counter such 'abuses', softer administrative measures would be appropriate, such as orders to cease the conduct. It is necessary to take into account the level of development of legal consciousness. In the future, when the level of legal awareness is higher, the definition of punishable behavior may become more severe. For now, it is important not to scare away our traders.

Acknowledgements

This article is supported by the Ministry of Education and Research within the framework of the project part of State Order for Research on Project No. 1503.

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