

# **Market Abuse Regulation in South Africa, the United States of America and the United Kingdom**

**Howard Chitimira**

Vernon Series in Law



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**To My Wife, Children and My Mother**

RACHAEL, ARIANA, NOLAN, NATHAN AND DIANA

You have been and still are my constant source of  
inspiration





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# Abstract

Market abuse (insider trading and market manipulation) practices have continued to cause various regulatory and enforcement challenges in several jurisdictions, including South Africa, the United Kingdom (UK) and the United States of America (USA). Accordingly, this book usefully unpacks the adequacy of the anti-market abuse laws and their enforcement in the aforesaid jurisdictions in order to isolate the flaws embedded in such laws and recommend possible remedial measures in respect thereof. This book offers a novel comparative analysis of the regulation and enforcement of anti-market abuse laws in two developed and renowned jurisdictions, namely, the UK and the USA as well as South Africa which has one of the biggest regulated financial markets in Africa. To my knowledge, there is no similar book that has been specifically written on the comparative regulation and enforcement of the anti-market abuse laws in these jurisdictions to date. To this end, the book provides the rationale for regulating and effectively combating market abuse practices in the USA, the UK and the South African financial markets. Notably, the book comprises of separate but related short papers that are provided in its nine chapters. For instance, Chapters Two to Five provide a comparative analysis of market abuse regulation in South Africa and the USA. Likewise, Chapters Six to Eight provide a similar analysis in relation to South Africa and the UK. Chapters Two to Eight were previously peer reviewed and published as journal articles and are now re-worked with permission from the initial publisher to update, expand and provide more recent information on the regulation and enforcement of anti-market abuse laws in South Africa, the USA and the UK. Such recent information includes, *inter alia*, the uncertainty surrounding the UK's anti-market abuse regime following its decision to withdraw from the European Union (EU) after the 2016 British EU (Brexit) referendum. Moreover, the recent South African and the USA international banks collusion and market manipulation involving the price-fixing, market allocation and rigging in the trading of foreign currency pairs of the South African rand since 2007 by lenders and banks is another reason for this book. A current surge of market abuse regulatory challenges caused by disruptive technology such as automated financial services, computerised trading, algorithms and artificial intelligence, especially, in the USA financial markets also influenced the writing of this book. Each Chapter has its own distinct title, introduction, relevant analysis, related conclusions and reference list. The

book equips the students, academics and other market participants with a simplified but updated and rich understanding of the regulation and enforcement of anti-market abuse laws in South Africa, the UK and the USA.

**Keywords:** insider trading; market manipulation; market abuse; regulation; enforcement approaches.

# Acronyms

BCBS	Basel Committee on Banking Supervision
CFTC	Commodity Futures Trading Commission
CFTF	Corporate Fraud Task Force
CPS	Crown Prosecution Services
DBERR	Department for Business Enterprise and Regulatory Reform
DMA	Directorate of Market Abuse
DPP	Director of Public Prosecutions
DOE	Division of Enforcement
DOJ	Department of Justice
DTI	Department of Trade and Industry
EBA	European Banking Authority
ECA	Economic Crime Agency
EC	Enforcement Committee
EDGAR system	Electronic Data Gathering Analysis and Retrieval system
EIOPA	European Insurance and Occupational Pensions Authority
EU	European Union
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
ERIC	Executive Regulatory Issues Committee
EDC	Executive Diversity Committee
EOC	Executive Operations Committee
FATF	Financial Action Task Force

FCA	Financial Conduct Authority
Fin-Net	Financial Crime Information Network
FPC	Financial Policy Committee
FINRA	Financial Industry Regulatory Authority
FERC	Federal Energy Regulatory Commission
FOS	Financial Ombudsman Service
FTC	Federal Trade Commission
FSA	Financial Services Authority
FSB	Financial Services Board
FSCA	Financial Sector Conduct Authority
FSCS	Financial Services Compensation Scheme
FSMT	Financial Services and Markets Tribunal
IFSG	Intermarket Financial Surveillance Group
IOSCO	International Organisation of Securities Commissions
JSE	Johannesburg Stock Exchange Limited
LSE	London Stock Exchange
LIFFOEAM	London International Financial Futures and Options Exchange Administration and Management
MOUs	Memoranda of Understanding
MSRMB	Municipal Securities Rule Making Board
MTFs	Multilateral Trading Facilities
MLAT	Mutual Legal Assistance Treaty
NASD	National Association of Securities Dealers
NYSE	New York Stock Exchange
NCA	National Crime Agency
NFA	National Fraud Authority

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LSE	London Stock Exchange
OTC	Over the counter
OTFs	Organised Trading Facilities
PA	Prudential Authority
PSC	Policy Steering Committee
PRA	Prudential Regulation Authority
UK	United Kingdom
USA	United States of America
RDC	Regulatory Decisions Committee
SFA	Securities and Futures Authority
SIB	Securities and Investments Board
SFO	Serious Fraud Office
SOCA	Serious Organised Crime Agency
SROs	Self-regulatory Organisations
SEBI	Securities and Exchange Board of India
STORs	Suspicious Transactions and Orders
STRs	Suspicious Transaction Reports
SEC	United States Securities and Exchange Commission
SEETS	Stock Exchange Electronic Trading Service
TPSE	Trade Point Stock Exchange
TRP	Takeover Regulation Panel
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union





## Chapter 1

# Introduction and Background

### 1 1 Introduction

Illicit insider trading and market manipulation (market abuse) practices<sup>1</sup> have given rise to several regulatory and enforcement challenges in many jurisdictions to date. Accordingly, these challenges have been, and are still being experienced in many jurisdictions such as the United Kingdom (UK), the United States of America (USA), South Africa and several other countries.<sup>2</sup> This could be attributed to a number of factors including, *inter alia*, the enactment of flawed market abuse laws and the use of few and less deterrent anti-market abuse enforcement approaches by the relevant enforcement authorities in many countries. Consequently, several anti-market abuse regulatory and enforcement authorities have grappled to effectively and consistently curb market abuse practices in their respective financial markets to date. The UK, the USA and South Africa were chosen to investigate and compare their respective anti-market abuse enforcement experiences. This was mainly done to isolate and recommend possible anti-market abuse enforcement approaches that could be employed in South Africa from both the USA and the UK's market abuse statutory regulatory frameworks. Accordingly, a brief comparative analysis of the enforcement of the market abuse prohibition in the UK, the USA and South Africa is undertaken in this book. It is hoped that this book will recommend possible measures that could be employed by the relevant enforcement authorities to improve the combating of market abuse practices in all the aforesaid jurisdictions.

The book discusses the adequacy of the market abuse prohibition in South Africa, the UK and the USA. Notably, market abuse is expressly prohibited at a national level in South Africa under the Financial Markets Act.<sup>3</sup> Likewise, market abuse is universally prohibited in the UK. Market abuse is also

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<sup>1</sup> Definitions and further discussions of these practices will ensue in Chapters Two to Eight of this book.

<sup>2</sup> Notably, this book is mainly focused on the comparative analysis of the regulation and enforcement of anti-market abuse laws in South Africa, the USA and the UK. It is hoped that this book will isolate and expose the gaps in the anti-market abuse regulatory frameworks in these jurisdictions in order to recommend where appropriate, possible measures that could be employed to remedy such gaps. See Chitimira *A Comparative Analysis of the Enforcement of Market Abuse Provisions* (Unpublished LLD thesis, Nelson Mandela Metropolitan University) 2012, 1-6.

<sup>3</sup> 19 of 2012 (Financial Markets Act). See ss 78; 80; 81 & 82.

outlawed both at a federal and state level in the USA.<sup>4</sup> Consequently, the offences, penalties and other anti-market abuse enforcement approaches that are provided in the relevant legislation of the stated countries are discussed in this book. The book also provides the rationale for regulating and effectively combating market abuse practices in the USA, the UK and the South African financial markets.

Notably, the book is comprised of separate but related short papers that are carefully spread over its nine chapters. Chapters Two to Five provide a comparative analysis of market abuse regulation in South Africa and the USA. Likewise, Chapters Six to Eight provides a similar analysis in relation to South Africa and the UK. Accordingly, Chapters Two to Eight were previously published as journal articles and are now re-worked with permission from the initial publisher to update, expand and provide more recent information on the regulation and enforcement of anti-market abuse laws in South Africa, the USA and the UK. For instance, such recent information includes, *inter alia*, the uncertainty surrounding the UK's anti-market abuse regime following its decision to withdraw from the European Union (EU) after the 2016 British EU (Brexit) referendum.<sup>5</sup> Moreover, the recent South African and the USA international banks collusion and market manipulation involving the price-fixing, market allocation and rigging in the trading of foreign currency pairs of the South African rand since 2007 by lenders and banks is another reason for this book.<sup>6</sup> The introduction of the Financial Sector Regulation Act<sup>7</sup> which introduces the Prudential Authority (PA) which supervises all financial institutions that provide financial products and securities services and the Financial Sector Conduct Authority (FSCA) which regulate the conduct of all financial institutions is another new information highlighted in the book.<sup>8</sup> A current surge of market abuse regulatory challenges caused by disruptive technology such as automated financial services, computerised trading, algorithms and artificial intelligence, especially, in the USA financial markets

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<sup>4</sup> Steinberg "Insider Trading Regulation—A Comparative Perspective" 2003 *The International Lawyer* 153 169-171; Chitimira "A Comparative Overview of the State Prohibition on Market Abuse in the United States of America" 2014 *Mediterranean Journal of Social Sciences* 54 54-68.

<sup>5</sup> This referendum was held on 23 June 2016. The majority of British citizens in that referendum voted to leave the EU. See SIA Partners (Banking and Insurance) "Brexit and the Impact on the UK's Regulatory Framework" (2016) 1-4 <<http://en.finance.sia-partners.com/brexit-and-impact-uks-regulatory-framework>> (accessed 12-07-2017); also see related comments in Chapter Six of this book.

<sup>6</sup> See further related remarks in paragraph 1 3 below.

<sup>7</sup> 9 of 2017 (Financial Sector Regulation Act) which was assented to by the President on 21 August 2017. However, the Financial Sector Regulation Act is yet to come into force on the day determined by the Minister of Finance by notice in the Government Gazette in terms of s 305 of the same Act.

<sup>8</sup> See Chapters 3 and 4 of the Financial Sector Regulation Act. Notably, the FSCA is set to replace the Financial Services Board (FSB).

also influenced the writing of this book.<sup>9</sup> Each Chapter has its own distinct title, introduction, relevant analysis, related conclusions and reference list. The author adopted this unique approach after receiving numerous requests from students, academics and other market participants who struggled to access all the initially published articles, hence the decision to re-publish them as a unitary book. The book equips the reader with a simplified but updated and rich understanding of the regulation and enforcement of anti-market abuse laws in South Africa, the UK and the USA.

## 1 2 Overview Background Aspects

Various effects of market abuse-related problems have been felt in the UK's financial markets from time to time. As a result, the UK has, from time to time, enacted some anti-market abuse laws in a bid to, *inter alia*, combat such problems and enhance the competitiveness of its financial markets. Accordingly, the UK employs a separate and specific statute that prohibits insider trading<sup>10</sup> and another statute that broadly prohibits market manipulation and other related market abuse activities.<sup>11</sup> Despite this, the anti-market abuse provisions of both the Criminal Justice Act and the Financial Services and Markets Act have relatively failed to effectively deter unscrupulous persons from continuing with their illicit market abuse practices in the UK's financial markets to date. This implies that both the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA)<sup>12</sup> which replaced the Financial Services Authority (FSA) have relatively failed to consistently enforce the anti-market abuse provisions to effectively combat market abuse activities in the UK's financial markets. Related market abuse problems have also affected the financial markets in the USA as early as the 1920s to date.<sup>13</sup> Similar problems were reportedly rampant in the South African financial markets between the early 1970s and the mid-1990s.<sup>14</sup> In a commendable attempt to curb the

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<sup>9</sup> Brummer "Disruptive Technology and Securities Regulation" 2015 *Fordham Law Review* 977-997-1003.

<sup>10</sup> See the Criminal Justice Act 1993 (c 36) (Criminal Justice Act).

<sup>11</sup> See the Financial Services and Markets Act 2000 (c 8) (Financial Services and Markets Act). See further Avgouleas *The Mechanics and Regulation of Market Abuse: A Legal and Economic Analysis* (2005) 307 and related discussions that ensues in Chapters Six to Eight of this book.

<sup>12</sup> These regulatory bodies replaced the FSA in accordance with the Financial Services Act 2012 (c 21).

<sup>13</sup> Chitimira *Enforcement of Market Abuse Provisions* 1-6, for further discussion and related discussions in Chapters Two to Five of this book.

<sup>14</sup> The South African financial markets had a very poor reputation due to rampant market abuse practices that occurred between the early 1970s and the mid-1990s. See Myburgh & Davis "The Impact of South Africa's Insider Trading Regime: A Report for the Financial Services Board" (25-03-2004) 11 <<http://www.genesis-analytics.com/public/FSBReport.pdf>> (accessed 09-02-2013); Chitimira "A Historical Overview of the Regulation of Market Abuse in South Africa" 2014 *PER* 937-937-939, for related comments.

negative effects of market abuse practices and related regulatory challenges, various anti-market abuse laws were introduced in South Africa from the early 1970s to date.<sup>15</sup> Nonetheless, despite these positive efforts, the South African anti-market abuse laws have been sometimes inconsistently enforced by the relevant authorities from the early 1970s to date.<sup>16</sup> For instance, previous anti-market abuse prohibitions that were contained in the Companies Act,<sup>17</sup> the Financial Markets Control Act,<sup>18</sup> and the Stock Exchanges Control Act<sup>19</sup> were both flawed and inadequately enforced by the regulatory authorities. Consequently, undeterred market participants and other relevant persons continued with their market abuse activities in both the regulated and unregulated South African financial markets.<sup>20</sup> The Insider Trading Act<sup>21</sup> was enacted to remedy the aforesaid flaws but its provisions were relatively inadequate and mainly limited to insider trading offences committed by individuals and not juristic persons. Moreover, its provisions did not expressly prohibit market manipulation.<sup>22</sup> The Securities Services Act<sup>23</sup> later repealed the Insider Trading Act and extended its market abuse prohibition to both insider trading and market manipulation and introduced administrative penalties which were enforced by the Enforcement Committee (EC) through the provisions that were inserted in the Financial Institutions (Protection of Funds) Act.<sup>24</sup> Nevertheless, its market abuse provisions were still relatively inadequate for deterrence purposes. The Securities Services Act was repealed by the Financial Markets Act which introduced relatively adequate defences, civil penalties for

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<sup>15</sup> See the discussions in Chapters Two to Eight of this book; Chitimira 2014 *PER* 937-965; Van Deventer "Anti-Market Abuse Legislation in South Africa" (10-06-2008) 1-5 <<http://www.fsb.co.za/public/marketabuse/FSBReport.pdf>> (accessed 05-05-2013); Myburgh & Davis (25-03-2004) 8-33, available at <<http://www.genesis-analytics.com/public/FSBReport.pdf>> (accessed 09-02-2013), for related comments.

<sup>16</sup> Scholtz, Paige & Van Zyl "Financial Markets, Market Abuse, Money Laundering and the National Credit Act" (31-03-2008) <[http://www.legal500.com/index.php?option=com\\_content&task](http://www.legal500.com/index.php?option=com_content&task)> (accessed 30-04-2016); Chitimira 2014 *PER* 937-965; Chitimira "Overview of the Market Abuse Regulation under the Financial Markets Act of 2012" 2014 *Obiter* 254-255-271.

<sup>17</sup> 61 of 1973 (Companies Act); see ss 162, 229-233.

<sup>18</sup> 55 of 1989 (Financial Markets Control Act); see ss 20-23.

<sup>19</sup> 1 of 1985 (Stock Exchanges Control Act); see s 40. Myburgh & Davis (25-03-2004) 8-33, available at <<http://www.genesis-analytics.com/public/FSBReport.pdf>> (accessed 09-02-2013), for related comments.

<sup>20</sup> Myburgh & Davis (25-03-2004) 11 available at <<http://www.genesis-analytics.com/public/FSBReport.pdf>> (accessed 09-02-2013); Chitimira 2014 *PER* 937-965, for related comments.

<sup>21</sup> 135 of 1998 (Insider Trading Act); also see "The King Task Group into the Insider Trading Legislation" 1995 (King Task Group); Chitimira 2014 *PER* 937.

<sup>22</sup> Ss 2-16 of the Insider Trading Act; Luiz "Market Abuse II-Prohibited Trading Practices and Enforcement" 2002 *JBL's Quarterly Law Review for People in Business* 180-183.

<sup>23</sup> 36 of 2004 (Securities Services Act). See ss 73; 75; 76 & 77.

<sup>24</sup> 28 of 2001 as amended (Protection of Funds Act). See ss 6A-6I of the Protection of Funds Act.

insider trading and maintained the administrative penalties regime.<sup>25</sup> However, more needs to be done to enhance market integrity and investor confidence in the South African financial institutions and financial markets by effectively curbing market abuse activities in these institutions and markets as discussed below.

### 1 3 The Rationale for Effective Market Abuse Regulation

Although it is still debatable<sup>26</sup> whether market abuse practices should be regulated,<sup>27</sup> the author submits that such practices must be statutorily and adequately prohibited in all jurisdictions to enhance the efficient and effective functioning of the financial markets. The effective regulation of market abuse enhances market integrity and public investor confidence in all jurisdictions. Moreover, the effective regulation of market abuse promotes free and fair financial markets that competitively attract foreign investment in several countries. The effective regulation of market abuse also promotes the creation and maintenance of transparent and efficient securities and financial markets where the price of a security accurately reflects its true value. Accordingly, the effective and consistent enforcement of adequate anti-market abuse laws by the relevant authorities is crucially important to the transparency and efficiency of such financial markets.<sup>28</sup> Thus, effective market abuse regulation in any country enhances the natural forces of supply and demand to accurately determine the price of securities in the financial markets of that country.<sup>29</sup> Put differently, anti-market abuse laws must be effectively enforced to promote market integrity, protect investors and to keep the financial markets free from market abuse activities and other illicit practices such as fraud.

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<sup>25</sup> Chitimira 2014 *PER* 937-939; Chitimira "Unpacking Selected Key Elements of the Insider Trading and Market Manipulation Offences in South Africa" 2016 *Journal of Corporate and Commercial Law and Practice* 24 24-41.

<sup>26</sup> For instance, some academics argue that the regulation of market abuse activities is economically undesirable, see Akerlof "The Market for 'Lemons': Quality Uncertainty and the Market Mechanism" 1970 *Quarterly Journal of Economics* 488 488-500; Ali "Market Abuse: It's Not just a Wall Street Thing" 2006 *The Company Lawyer* 222 224; Fischel & Ross "Should the Law Prohibit 'Market Manipulation' in Financial Markets" 1991 *Harvard Law Review* 503 512-513 & 553. On the contrary, other commentators argue that the effective anti-market abuse legislation is vitally important to accurate and internationally competitive financial markets in all jurisdictions. See Chitimira *Enforcement of Market Abuse Provisions* 6-13; Anonymous "The Regulation of Insider Trading in the United States of America" (09-03-2008) <<http://www.sec.gov>> (accessed 08-06-2016).

<sup>27</sup> Henning & Du Toit "The Regulation of False Trading, Market Manipulation and Insider Trading" 2000 *Journal for Juridical Science* 155 155-165; Chitimira *Enforcement of Market Abuse Provisions* 6-13; Gething "Insider Trading Enforcement: Where are We Now and Where do We Go from Here?" 1998 *Company and Securities Law Journal* 607 607-627.

<sup>28</sup> Henning & Du Toit 2000 *Journal for Juridical Science* 155-165; Chitimira *Enforcement of Market Abuse Provisions* 6-13.

<sup>29</sup> Chitimira *Enforcement of Market Abuse Provisions* 6-7.

Moreover, the effective enforcement of anti-market abuse laws enhances the combating of market abuse activities that are still occurring in many jurisdictions, including the USA, the UK and the South African financial markets and financial institutions.<sup>30</sup> For instance, the ineffective enforcement of the anti-market abuse prohibition has culminated in a relative surge of market abuse activities in the South African financial institutions and financial markets in the recent years. The recent South African, the USA and other international banks collusion and market manipulation involving the price-fixing, market allocation and rigging in the trading of foreign currency pairs of the South African rand since 2007 by lenders and banks such as the Bank of America Merrill Lynch International Limited, JP Morgan Chase and Co, JP Morgan Chase Bank N.A, Macquarie Bank, BNP Paribas, Credit Suisse Group, HSBC Holdings, Commerzbank, Australia, New Zealand Banking Group, Barclays Capital and Barclays, Standard New York Securities and Nomura Holdings International is a case in point.<sup>31</sup>

Consequently, it is less prudent to assume that the enactment of adequate market abuse laws alone will automatically combat market abuse activities and give rise to increased market integrity and investor confidence in the USA, the UK and South African financial markets.<sup>32</sup> On the contrary, such laws will only effectively curb market abuse activities if they are robustly and consistently enforced by the relevant enforcement authorities. In other words, adequate anti-market abuse legislation alone is not sufficient since such legislation must be supplemented by effective enforcement of its provisions to combat market abuse practices. In a nutshell, adequate anti-market abuse laws must be consistently enforced in all the jurisdictions to enhance the integrity and efficiency of the financial markets.

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<sup>30</sup> *Pather and Another v Financial Services Board and Others (57617/10)* [2014] 3 All SA 208 (GP), for related discussion on the role of the EC; *Zietsman v Director of Market Abuse* 2016 1 SA 218 (GP), which dealt with the meaning of “inside information” for the purposes of the insider trading offence in South Africa; the Directorate of Market Abuse (DMA) “Past Investigations” *DMA Media Release* 23 June 2015, 1-11; the DMA “Report by the Directorate of Market Abuse” *FSB Press Release* 31 March 2017, 1 1-3.

<sup>31</sup> Anonymous “How Banks Allegedly Colluded on Currency Trades” (15-02-2017)

<<http://www.fin24.com/Companies/Financial-Services/why-the-competition-commission-wants-17-banks-prosecuted-20170215>> (accessed 21-03-2017).

<sup>32</sup> For instance, see Anonymous “Steinhoff, Brait Share Movements Probed for Insider Trading” (25-06-2015) <<http://www.fin24.com/Companies/Financial-Services/Steinhoff-Brait-share-movements-probe-d-for-insider-trading-20150625>> (accessed 21-03-2017); Burkhardt “Insider Trading Rocks SA Coal Mine” (15-03-2017) <<http://www.fin24.com/Companies/Mining/insider-trading-rocks-sa-coal-mine-20170315>> (accessed 21-03-2017); Anonymous “JSE to Investigate MTN for Possible Insider trading” *Fin24* (30-10-2015) <<http://www.timeslive.co.za/local/2015/10/30/JSE-to-investigate-MTN-for-possible-insider-trading1>> (accessed 21-03-2017); the DMA “Report by the Directorate of Market Abuse” *Financial Services Board (FSB) Media Release* 30 March 2016, 1 1-3, for further examples of market abuse activities that have been recently reported in the South African financial markets.

#### 1 4 Concluding Remarks

Illicit market abuse practices may, *inter alia*, give rise to poor integrity and efficiency of the financial markets in any country where such practices are rampant. These and other negative effects have either directly or indirectly affected the normal functions of the financial markets in the USA, the UK, South Africa and other countries to date.<sup>33</sup> Market abuse-related problems have continued to be exacerbated by either the enactment of inadequate anti-market abuse laws and/or the inconsistent enforcement of such laws in many countries, including South Africa, the UK and the USA.<sup>34</sup> Given this background, it is submitted that South Africa, the UK, the USA and other countries must adopt a robust approach to regulate and effectively combat market abuse practices in their respective financial markets.<sup>35</sup> Accordingly, this book exposes the need for the enactment of adequate anti-market abuse laws as well as the robust enforcement of such laws in many jurisdictions as discussed above. This approach enhances and promotes competitive and efficient financial markets across all the jurisdictions.

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<sup>33</sup> See paragraph 1 2 above.

<sup>34</sup> See paragraph 1 2 above.

<sup>35</sup> See paragraph 1 3 above.

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