

CANADIAN SECURITIES ADMINISTRATORS

Alternative Trading System Proposal

**Written Submission
of the
Commissioner of Competition,
Competition Bureau**

September 2000

As part of an initiative to create a framework that permits the competitive operation of traditional exchanges and Alternative Trading Systems [“ATSS”], the Canadian Securities Administrators [the “CSA”] published in July 1999 an Alternative Trading System Proposal. In response to comments received from a substantial number of commenters, the CSA republished for comment a revised proposal in July 2000.

In response, the Commissioner of Competition, Competition Bureau, [the “Commissioner” or the “Bureau”] submits the following points to the CSA for consideration.

In addition to enforcing the various provisions of the *Competition Act*, the Commissioner has a statutory function, pursuant to sections 125 and 126, to intervene before federal and provincial regulatory boards, commissions and tribunals to make representations concerning competition. The Commissioner also has a policy role as advisor to government on competition matters. As such, the Commissioner has made frequent submissions to legislative committees. Making such interventions gives the Commissioner an opportunity to ensure that competitive factors are taken into consideration in the formulation of various policies.

The Bureau welcomes this opportunity to provide its views on the CSA initiative. Specifically, the Bureau wishes to respond to Question 2 from the CSA’s Specific Requests for Comment concerning the provision of market regulation for ATSS in the equity market. The submission outlines a number of considerations that from a competition policy perspective bear on the question of who should provide market regulation for ATSS.

There is good reason to believe that competition between stock exchanges and ATSS is in the best interest of consumers, the securities industry and the Canadian economy. The Bureau believes that a regulatory environment allowing for competition among markets will stimulate innovation and encourage markets to be more responsive to the needs of participants. Experience throughout the economy attests to the considerable benefits of relying on competition to promote economic efficiency.

The Bureau recognizes that industry self-regulation can also provide important benefits in the public interest. Market forces alone cannot always guarantee appropriate standards of conduct, competence and integrity. Therefore, the Bureau does not oppose, in principle, industry regulation which can complement the *Competition Act* in establishing appropriate rules of conduct. However, self-regulation involves particular risks for the competitive process. So as to take full advantage of the benefits of both industry self-regulation and competition, the Bureau believes that the following matters are important considerations in the development of any industry self-regulatory process.

Regulation should clearly and effectively address legitimate concerns without unnecessarily restricting competition. Regulations should be reasonably necessary for the protection of the public and should not restrict competition any more than is needed to achieve the desired objectives. It is important that regulation not hinder competition by, for example, imposing

excessive compliance costs. For regulations to be socially beneficial, the benefits of regulation must at least outweigh the direct costs to businesses.

To this end, a regulatory scheme should include objectives clearly stating the reasons for its being established and the outcomes it intends to achieve. Rather than simply presenting broad general principles, the scheme should address specific, stated problems and include performance standards. Another way to help minimize unnecessary or overly restrictive regulation is to make the promotion of competition a primary objective for an SRO.

A primary objective of the regulatory framework should be to promote open and effectively competitive markets. Open and effective competition provides the most generally effective means to promote the efficient, low cost and innovative supply of products meeting consumers' tastes and needs. Except in cases involving natural monopolies, or where such competition is not feasible for other reasons, the Bureau supports the promotion of open and effective competition as a key goal of regulation.

In the Bureau's view, a market may be considered open and effectively competitive if the following conditions are met: (i) all potential competitors have the ability to compete, subject to any necessary technical, safety or other such requirements, based on their costs and ability to meet consumer demands at a lower price; and (ii) no participant in the market has sufficient market power to profitably sustain a significant and non-transitory price increase. Only where these conditions are met can competition be expected to provide the maximum benefits in terms of low prices and the efficient use of economic resources.

The regulatory environment should neither favour nor constrain the ability of particular market participants to compete in the market. In all markets, there will be some businesses that are more effective competitors than others. A regulatory environment should not try to offset these differences or in any way try to establish equality among competitors. Rather, it should provide a market framework within which all firms thrive or fail on the basis of their ability to meet consumers' demands at the best combination of price and quality. Only where such conditions exist will the efficient allocation of output among competing suppliers be possible, and total welfare be maximized.

The regulatory process must be impartial and not self-serving. To accomplish this, the governing body must broadly represent all aspects of the industry being regulated. No single class of persons should dominate the governing body. This will ensure that no particular market participant or group of market participants will be able to control the regulatory process and manipulate it to their advantage.

Governance of the SRO should ensure the transparency of self-regulatory activities. Independent public membership should at least balance industry representation on the SRO's board of directors. In addition to consumer or user representation, the public directors should include

representatives of the appropriate regulatory authority. Such representation helps ensure that self-regulatory activities are in the broader public interest by providing a public window on the SRO's operations.

The SRO should institute a formal complaint handling process. The SRO should make provision for the lodging and handling of complaints with respect to the full range of its activities and responsibilities. It should incorporate performance criteria that provides a standard for effective complaints handling. The regulatory authority overseeing the SRO should provide independent review of complaint handling decisions as required.

A regulatory scheme should allow for periodic assessment of its effectiveness and be subject to regular reviews. The SRO should produce annual reports on its activities and provision should be made for regular reviews to ensure that the regulatory scheme is effectively meeting current needs.

Care must be taken when delegating enforcement powers to industry self-regulatory organizations. It is important to ensure that such powers cannot be used to restrict competition among incumbents any more than is necessary, or to erect any unnecessary barriers to entry by new competitors.

The Bureau supports the CSA's initiative to create a framework that permits the competitive operation of traditional exchanges and Alternative Trading Systems. Allowing for competition between markets will promote the efficient, low cost and innovative provision of services. The Bureau believes that having regard to the above considerations will help ensure that the potential benefits of competition are fully realized.

This concludes the Bureau's submission. The Bureau thanks the CSA for this opportunity to respond to the ATS Proposal.

Competition Bureau
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