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# The Case for a Common Capital Markets Regulator

## The Case for a Common Capital Markets Regulator

### Introduction

The financial sector is integral to Canada's economic success. It contributes \$85 billion to the Canadian economy annually and provides 750,000 direct jobs and 800,000 indirect jobs, many of them high-skilled and high-paying. Just as importantly, the financial sector supports the growth of all other sectors of the economy by connecting savers with businesses that need to make productive investments and by helping people and businesses transfer risks to others who are better equipped to manage those risks.

Within the financial sector, the capital markets play an essential role. When capital markets function well they provide wider opportunities for individuals to invest their savings and for businesses, large and small, to raise capital and manage risks. They can also be subject to fraudulent, abusive and unfair practices, and can transform and transmit risks that threaten financial stability and economic prosperity.

By being responsive to national and international stresses to financial stability, by building the capacity to respond effectively to market innovations, and by strengthening our enforcement regime, a Common Capital Markets Regulator (CMR) would be well-positioned to address the challenges of tomorrow's capital markets.

Canada already benefits from world-leading banking regulation. These benefits are both direct, from efficient and reliable provision of banking services, and indirect, from the strong international reputation of Canadian regulation and Canadian banks. s.16

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### The challenges ahead

Canadian capital markets have changed profoundly in recent years and the rate of change is accelerating. Our capital markets regulatory system faces four key challenges in the years ahead.

#### *Adapting to change*

Capital moves freely around the world, in parallel with the growth of international trade and investment. Advances in technology and increased competition have created alternative trading systems to compete with traditional stock exchanges, which themselves have been transformed from not-for-profit national or regional utilities into internationally competitive enterprises. Computerized strategies allow traders to rapidly move in and out of securities positions and innovative financial engineering is continually creating new and complex types of securities and derivatives. Hedge funds, sovereign wealth funds, and private equity firms have changed the face of the investor community while dealers, advisers, and fund managers have changed their business models. Meanwhile, the growth of online trading and communications is making complex and

risky financial products available directly to retail investors, adding to the challenge of ensuring that they are adequately protected.

These changes have created new opportunities for investors and market participants, s.16,s.17

Regulators around the world are trying to understand the implications of all these new developments and, as a consequence, many are investing in increased analytical capabilities and broader skill sets. s.16,s.17

### *Managing systemic risk*

We should not underestimate the challenge of devising capital market regulation that supports financial stability. s.16,s.17

The crisis showed that broader systemic risks, previously thought to be largely confined to the banking sector, can also arise in capital markets. s.16,s.17

### *Enforcement*

Regulation can be effective only if it is backed up by an effective system to enforce compliance. s.16,s.17

Sophisticated financial wrongdoers, in Canada and abroad, are constantly finding new ways to cheat investors of their money. They have become adept at using technology and operating across multiple jurisdictions to evade regulation and enforcement. s.16,s.17

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*Supporting economic competitiveness and growth*

Capital markets play a crucial role in helping Canadian businesses raise the funds they need to make productive investments. <sup>s.16</sup>

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How can we ensure that Canada's capital markets regulatory regime meets these challenges?

**A common capital markets regulatory regime**

Canada can best meet the challenges facing our capital markets regulatory regime by pooling federal and provincial jurisdiction and resources to create a common capital markets regulator administering a single legislative and regulatory framework. A common Capital Markets Act would apply in all participating jurisdictions. Some elements would apply across the entire country, notably the criminal provisions and measures related to managing systemic risk and maintaining the integrity and stability of Canada's financial system.

The CMR would have an accountable, integrated governance and management structure in which executives and staff in various provinces would become colleagues. This key advantage would enable regional perspectives and concerns to be identified quickly and brought to the table by CMR colleagues and market participants within each CMR jurisdiction.

Establishing a common regime would make Canada's capital markets more internationally competitive and better support economic growth. The adoption of common legislation and rules would eliminate the regulatory costs currently borne by market participants to keep track of and comply with differences between jurisdictions. The CMR would also enable the establishment of a single, simplified and lower overall fee structure for market participants. Both of these changes would help reduce the cost of capital in Canada, stimulating productive investment. Combined with a strengthened enforcement regime, this would enhance our ability to attract foreign issuers and make Canada an appealing destination for foreign investment. Greater business investment, in turn, would make the domestic economy stronger and more competitive. <sup>s.16</sup>

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s.16                      The greater analytic capacity of a CMR would also enable more timely policy responses to emerging national and international issues. <sup>s.16</sup>

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To support financial stability, the CMR would have a national data collection power and powers to impose rules and orders consistently across the entire country to prevent risky practices and respond to disturbances arising from anywhere in Canada or from beyond our borders. The CMR would provide a single point for coordination with other financial sector regulatory authorities. This interaction would provide other regulators with a comprehensive perspective on Canada's capital markets and give the CMR access to information that would permit it to identify and respond to emerging threats s.16

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The CMR would also support the comprehensive enforcement capacity needed to quickly detect and take action against misconduct spanning multiple provinces. A common database would contain information obtained from surveillance, complaints, compliance reviews, and investigations, providing staff in any office with the tools to detect market abusers. Investigations could be pursued without regard to provincial boundaries or the location of witnesses or evidence. Staff with specialized expertise would be available to assist in investigations conducted by any office, to ensure that consistent standards and approaches are applied and that the most current knowledge is brought to bear on each case. CMR staff could apply to the independent tribunal for administrative orders that would apply nationally, or they could refer matters to federal or provincial prosecutors to seek criminal or regulatory sanctions through the courts.

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