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International Experience of Competition Regulation on the Securities Markets

Keywords: *competition, regulation, stock market, primary dealers, insider information.*
Annotation: *In the paper experiences of different countries in aspect of securities market regulation and creation a competitive environment on the market is considered. The practice of the highly developed countries such as United States, Germany, Canada, China, was analyzed. Key provisions in the competition legislation of these countries, which may be applied by the developing countries in order to create a fair business environment and to prevent anticompetitive actions on the securities market, are researched. The basic principles on which the selection of primary dealers is providing in different countries are analyzed.*

Fair competition between market players is the basis of just pricing and creates the conditions for the realization principles of the optimal structure of the stock market. Conditions of perfect competition must be observed between the numbers of market members: stock exchanges, brokers, dealers, investors, banks (for the opportunity to be primary dealers), depositories (custodians and registrars) of the securities. The principles of transparency and fair competition between them are shown, as in price (cost reduction on services) and non-price competition (differentiation of types of the services that are providing by them, and improving the quality of such services, aggressive advertising campaign etc.).

In view of the above said, the regulation of competitive relations is a complex task that encompasses the full range of activities - from complete economic restructuring to creation the traditions of civilized market relations and conditions for a stable and secure ménage, introduction a transparent and open mechanism of the domestic economy protection and unfair competition prevention.

The global economic crisis of 1920-1930's, the Great Depression of 1929-1933 demonstrated the consequences which leads liberal approach of neoclassical school, according to which the mechanism of free competition and market pricing provides equitable distribution of incomes and full use of economic resources.

Modern markets through the impact of the monopolies and oligopolies on them are noncompetitive, and therefore unable to regulate supply and demand automatically, especially it deals the correlation between prices and wages. As the market is incapable to full self-regulation, state should be an active participant that provides this task. Such beliefs was adhered by John Maynard Keynes.

Special attention should be paid to the stock market regulation, which is greatly exposed to adverse fluctuations of the unstable external financial environment. The stock market should facilitate the circulation and rational allocation of financial resources, to provide the opportunity evaluate the effectiveness of their use, to create the conditions for

fair competition and restriction of monopolistic phenomena. According to this, the establishment and functioning of holistic, highly liquid, efficient and fair securities market in the developing countries is impossible without proper regulation.

Regulation and self-regulation. A well-functioning capital markets are a sign of the developed economies. In order for the economy was growing, companies should be capable to accumulate funds and get some benefit from the growing opportunities of the resources accumulation. Enterprises are increasing their funds at the capital markets and for putting money into the companies, investor must trust the information that is available about them.

The market may collapse in the absence of such trust. A striking example of this was the Great Depression in the United States. During 1920-s, was issued about $ 50 billion of securities. By 1932, half had become worthless. The public's confidence in the capital markets justifiably plummeted, and lawmakers agreed that for the economy to recover, public faith had to be restored. Following a series of investigative hearings, Congress passed the Securities Act of 1933, and shortly after the Securities Act of 1934. The main purpose of these laws was to (1) require firms to tell the public the truth about their businesses, and (2) require brokers, dealers, and exchanges to treat investors fairly. Congress established the Securities and Exchange Commission (SEC) to enforce these laws (1).

As a result, in the 30's in the U.S. has developed a two-tier system of securities market regulation. Level 1 - the authorities of government regulation, primarily SEC and special regulators in the states, 2nd level - self-regulatory organization of professional participants at securities market, among them primarily are stock exchanges and SROs (regulatory organization at financial industry).

Herewith the SEC is the primary regulator (as the Americans say, watchdog) of the U.S. stock market. It has a wide range of responsibilities even may conduct its own investigation, calling witnesses to testify. In addition, because of the importance of the stock market in the U.S. economy, the regulator is traditionally more powerful authority than similar regulators in other countries. As indicated on the official website of SEC the mission of the U.S. Securities and Exchange Commission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation (2)**.**

Thus, objective could be achieved by providing constant and accurate flow of information to investors on which they rely deciding whether investment in securities is rational or not. Thus the Commission is mainly focused on promoting information disclosure and reducing its asymmetric information in order to ensure equal, competitive conditions for all market participants. Giving a great importance to self-regulation for professional market participants, SEC is able to transfer its powers to them and increase the efficiency of their resources use in such way.

The largest self-regulation organization on the U.S. stock market is the Financial Industry Regulatory Authority (FINRA) established after the merger of the National Association of Securities Dealers and Committee of the New York Stock Exchange regulation.It's responsible for managing business relationships between brokers, dealers and investors. FINRA is not part of the government. It an independent, not-for-profit organization authorized by Congress to protect America's investors by making sure the securities industry operates fairly and honestly (3). The north U.S. neighbor - Canada has another approach.

In general, the Canadian stock market is an essential element of the financial and credit system of the country, and occupies a crucial place that ensures the savings transformation into investment. Primary responsibility for regulation in the securities industry is on the provincial governments.

Heads of Securities Commissions of all Canadian provinces and territories are united in an informal voluntary organization - The Canadian Securities Administrators (CSA), objectives of which is to protect investors' rights, promotion an effective system of Canadian securities market transparency and to give proposals of measures to reduce systemic risk on the financial market (4).

Especially useful for developing countries in part of reducing the number of supervisory institutions, resources concentration, avoiding interaction problems and speeding up the regulation process will be German experience, where all regulation authorities of financial markets are consolidated in one supervision body

Since May 2002 into the general regulation institution had combined federal agency of financial institutions supervision, the federal office for of securities trading supervision, the federal chamber of banks supervision.

The reason of the consolidation was the emergence of financial conglomerates that combine banks, insurance companies and other financial institutions, and as a result, the growing integration of financial markets. Therefore the guarantee of the financial markets stability for a long time is a comprehensive financial supervision. This federal government agency is organizationally independent, but legally subordinated to the Federal Ministry of Finance of Germany. Thus it is independent of the federal budget (5).

In the part where it’s costs does not covered by the charges and compensation payments, they are paid according to the allocation formula by organizations that are the subject of supervision by the regulator, such as banks, insurance companies, organizations that provide financial service, brokers and other market participants admitted to the stock exchange, as well as local issuers whose securities are traded on them.

Competition law. For development of any economy sphere, fair and equal facilities must be provided for all participants of economic activity. All this must be reflected in competition legislation. It should be noted, that to ensure transparent functioning and creating an effective competitive environment, the U.S. Congress adopted a series of legislative acts that significantly contributed to the development of U.S. stock market transparency.

In 1977, Congress accepted Foreign Corrupt Practices Act, supervision of its execution was entrusted to the SEC. Under this law, was prohibited to bribe government officers and politicians abroad by the officials of the american corporations. Companies convicted in violating this law may be fined, officials - fined up to 100 thousand dollars or even imprisonment for up to 5 years (or both simultaneously).The same law provides, that statements of public companies must accurately reflect all transactions and to prevent the presence of unaccounted funds "black cash" (6).

The result of this law - numerous investigations by the SEC and the liability of companies who have been committed offenses. As na example the SEC alleges that employees and agents of Pfizer’s subsidiaries in Bulgaria, China, Croatia, Czech Republic, Italy, Kazakhstan, Russia, and Serbia made improper payments to foreign officials to obtain regulatory and formulary approvals, sales, and increased prescriptions for the company’s

pharmaceutical products. They tried to conceal the bribery by improperly recording the transactions in accounting records as legitimate expenses for promotional activities, marketing, training, travel and entertainment, clinical trials, freight, conferences, and advertising. The SEC separately charged another pharmaceutical company that Pfizer acquired a few years ago – Wyeth LLC – with its own FCPA violations. Pfizer and Wyeth agreed to separate settlements in which they will pay more than $45 million combined to settle their respective charges .In 2011, the SEC filed charges to "Johnson & Johnson" for bribing doctors in some European countries, in order to obtain contracts of their products purchase. The company paid a fine of $ 70 million to meet all claims that have been filed (7).

In practice of the U.S. antitrust laws often enough, the principle of balanced approach is used. Thus, for a conviction, the judge should not only confirm the illegal activities, but also he needs to accept the evidence that the loss of negative effects on competition dominated received benefits for economy.

The popularity of the « rule of reasonableness » as the principle of applying antitrust law was increasing in the U.S. since the mid 1970's to early 1990's. This coincided with the expansion of the use of the new, combined forms of agreements in the economy (including franchising). Application of antitrust laws basing on «balanced approach», in contrast to the strict following of law provisions, generally regarded as a less severe punishment. However, in the last fifteen years, is another trend - not crowding one principle by another, but a clear distinction between the circumstances of their application such practice widely used in Europe.

In regard to competition law in Germany, the basic normative document that regulates unfair competition is the Law about Unfair Competition (Gesetz gegen den unlauteren Wettbewerb (UWG, 2004)). In the part of the law about Unfair Competition is stipulated that the actions that display the unfair competition are prohibited if they can significantly affect on the competitors' interests, consumers or other market participants.

In accordance with the provisions laid down in the law, commercial activity, in which consumers are involved in, is unfair if such activity is contrary to the requirements of professional rectitude and can significantly affect on the ability of consumers to make an informed decisions about the transaction and thus force them to make a decision, which they otherwise would not done. Also prohibited are transactions that generate false or misleading signals affecting supply, demand or price of a financial instrument – including, among other things, the unfair trading practices of wash trades or pre-arranged trades. But other deceptive acts also constitute market manipulation if they have the potential to influence the price of a financial instrument – for example, if an investment adviser buys shares and then recommends them as a "buy" solely to drive the price up und sell them again at a profit (scalping) (8).

Manipulations that have demonstrably influenced the stock exchange or market price are criminal offences punishable by a term of imprisonment of up to five years or a fine. During the supervision of market entities concentration, such operations are controlling (9):

- complete assets acquisition;
- company shares purchase in volume of 25, 50 percent or more;
- any transaction as a result of which the firm acquires direct or indirect control over the company

– any agreement, including the purchase of at least 25 percent of the shares if it allows the buyer to influence the competitive behavior of other firm.

In general in the European Union powers to protect competition, competition policy formation and its implementation entrusted to the General Directorate of the European Commission. In some cases, these functions may be distributed among the competent authorities that are responsible for the competition regulation in the states -members of EU and legislative courts. Today, all states-member of EU carry out a common policy in the field of competition, which is characterized by a perfect and rational mechanism of its implementation an highly effective control of competition compliance.

Information disclosure and Insider information. Great attention is paid to insider information and how it can influence on the competition level, in legislation of USA. In the 80th were accepted two laws that increase penalties against insiders for the use of inside information – Insider Trading Sanctions Act 1984, Insider Trading and Securities Fraud Enforcement Act 1988.

Previously, the SEC could confiscate only proceeds that where derived from the use of inside information. In accordance with these laws fine may exceed 3 times the profit gained from the use of inside information. An insider can be imprisoned up to 10 years. In addition the system of people stimulation, which inform about the facts of illegal use of insider information, was provided (10).

Stock market regulation system in China created like in the U.S. A specialized government body was established, for centralized stock market control. In the PRC regulator is the Commission of Securities market Regulation provided at the State Council of the PRC in 1992. Model of the stock market regulation in China is a system of strict principles imbued from the U.S. practice, which is characterized by strict regulation and mandatory implementation of administrative procedures to the issuance of securities and their admission to trading (11).

Regulation of primary market and, in particular, underwriting, in China also formed including the U.S. practice of using the mechanism of «due diligence» («due diligence» - proper compliance) – that means that underwriter checks the correctness, completeness and accuracy of application documents that issuer represent, and also promoting the formation of proper reporting system within the consultation period. In this way China's Commission also provides more rigid regulation. In particular, the envisaged liability of underwriter (up to the revocation of a license) in case of detection the false information about the issuer in preparing, placing, and in the case of fraud reporting, a sharp deterioration in the financial situation of the issuer and committing affiliated transactions within two years after the IPO.

What deals the inside information, In China for its trading provided compensation up to five times bigger than the amount of profit that was achieved. Also is possible occurrence of criminal responsibility. In particular, at the end of 2007 during its existence Commission investigated 405 cases of violations, and 32 of them were transferred to criminal proceedings (12).

Very interesting and useful is experience of Canada in the sphere of information use and disclosure. According to the Canada Business Corporations Act 1985, the investor who receives 10 percent or more of the shares of any class at Canadian companies should inform about his intentions to the Securities Commission in respective province of Canada. All shareholders that control directly or indirectly 10 percent or more of the shares in Canadian companies are marked as insiders of the company (4).

Also must be declared an increasing insider's case of shares on 2% or more. For the purpose of bigger efficiency of information disclosure system, in the securities market, and for promoting insiders of Canadian companies working with local regulators, CSA (Canadian Securities Administrators) members have developed a system of electronic information disclosure by insiders – System for Electronic Disclosure by Insiders (SEDI), which reduces the time and facilitates large shareholders of Canadian corporations filing process of required documents and their transfer to the appropriate securities commission.

Primary dealers. Primary dealers operation is typical for many countries. Accordingly, each state has its own policies and principles concerning the regulation and ensuring a competitive environment in the area of primary dealership. An important aspect in a transparent and competitive activity of a primary dealership is to have certain criteria that applicants must meet to be considered as primary dealer (table 1).

Table 1

Selection Criteria of primary dealers in different countries

State	Basic requirements for banks that claim to become a primary dealers of the state securities
1	2
U.S.A	A prospective primary dealer should be prepared to demonstrate to the New York Fed its activity levels in the various markets in which the New York Fed's domestic trading desk transacts. A prospective dealer must be able to demonstrate an ability to provide sizable, sustained performance in operations A primary dealer must be either a broker-dealer4 registered with and supervised by the Securities and Exchange Commission (SEC) or a U.S.-chartered bank (commercial bank, thrift, national bank or state bank) that is subject to official supervision by bank supervisors. The primary dealer must meet certain minimum capital requirements: 1. A registered broker-dealer must have at least $150 million5 in regulatory net capital as computed in accordance with the SEC's net capital rule.6 The broker-dealer must otherwise be in compliance with all capital and other regulatory requirements imposed by the SEC or its self regulatory organization (SRO). 2. A bank must meet the minimum Tier I and Tier II capital standards under the applicable Basel Accord and must have at least $150 million of Tier I capital as defined in the applicable Basel Accord (13,14).
Spain	Entities must: - to be holders of a securities account in their own name in the Public Debt Market in Book Entries. - to fulfil the requirements that are established in terms of the provision of technical and human resources, as well as satisfy the other financial and legal conditions that are required in order to be classified as members with full faculties in at least one of the regulated markets or multilateral trading systems determined by the General Directorate of the Treasury and Financial Policy. - To be active during a minimum period of one month, demonstrating through their activity in the primary and secondary markets in Treasury Bills that they have a commitment to the Spanish market in public debt similar to that required of all Market Makers (15).

Czech Republic	A Primary Dealer is required to fulfill the following criteria at the time of submitting the application: in the 6 months period preceding submitting the application it has participated, through one or more Primary Dealers, in auctions and has subscribed for at least 3 % of the total face value of Czech Government Bonds on a duration weighted basis allocated in this period by the Ministry of Finance on a competitive basis, to be an active DETS participant for at least 6 months period preceding the submitting the application and to have a past record of active secondary trading of the Czech Government Bonds. To act as Primary Dealer (or similar one) for at least three other European Union member states at the same time (applicable to non-resident institutions),in the opinion of the Ministry of Finance, maintain highest standards in financial business practice, consistent with the Ministry of Finance's objective of achieving orderly, efficient and liquid Czech Government Securities market (16).
Greece	The selection of Primary Dealers takes place once a year based on the following criteria: 1. To have a minimum net worth of EUR 375 million. For Greek branches of foreign credit institutions, as “net worth” is considered the net worth of their parent in the home country. 2. To have an organized unit (Dealing Room and Back Office) in order to trade efficiently in the securities market and to abide by the obligations of Primary Dealers. 3. For the selection of Primary Dealers, the participation in HDAT, EuroMTS and other regulated market according to the definition under MiFID shall be taken into account in order of precedence and cumulatively as quantitative criteria (17).

As we can see the main point is financial strength is evidenced by adequate capitalization. It generally translates into a minimum net worth requirement. Being a primary dealer is a risky business. In the primary market, a primary dealer may end up holding a large securities portfolio which is either too expensive or not saleable. Market conditions may have changed after the auction or the primary dealer may have misjudged market pricing or investors demand. Similarly, in the secondary market, a primary dealer may have bought securities at a high price or sold too cheap. As a result, losses may be suffered, with the corresponding need for a capital cushion to absorb them. The financial strength requirement has some additional advantages. It restricts the function of primary dealers to the soundest institutions and limits the risk of future financial problems of primary dealer.

Conclusion. So summarizing research that was done, we can make a conclusion, that for an efficiency regulation, a securities market regulation institution must be given a full functional range as it done in the U.S. Also very effective is to consolidate the overall supervision of financial markets in a single institution, as in Germany, in such way it provides a quickly information sharing, decision making and efficient problems solving.To ensure competitive environment on the market, extremely important is to provide control under the inside information and anticompetitive actions. Quite effective mechanism in these aspects created in the U.S., Germany and Canada. Where, regulation of the firm’s ability to influence on the market situation is lay down into the basis of the regulatory mechanism.What deals a primary dealer system, the study of international practice in this matter, shows that for establishment the competitive network of government securities sellers is necessary to provide their quality selection. It should be based on the such criteria as volume of capital; term and government securities trading volume, ability to sell a certain amount of government securities. Thus,

developing countries for the formation of their own, effective regulation system of the securities market that would ensure functioning and maintenance the quality competitive environment it is necessary to consider and adapt the practice of foreign countries, where such systems operate for a long period.

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