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# I. INTRODUCTION

1. Singapore Exchange Limited ("***SGX***") welcomes the opportunity to submit its comments on the draft of the proposed Competition Bill (the "***Bill***").

2. SGX's comments are also made on behalf of SGX's wholly-owned subsidiaries, namely, Singapore Exchange Securities Trading Limited ("***SGX-ST***"), Singapore Exchange Derivatives Trading Limited ("***SGX-DT***"), the Central Depository (Pte) Limited ("***CDP***"), and the Singapore Exchange Derivatives Clearing Limited ("***SGX-DC***"), and the businesses that they operate.

3. The comments set out herein by SGX are in response to the first round of the public consultation of the Bill issued by the Ministry of Trade & Industry ("***MTI***") on 12 April 2004.

4. SGX's submission is set out in the following manner:

   (a) Part I contains this Introduction;

   (b) Part II contains a summary of this submission;

   (c) Part III contains SGX's statement of interest;

   (d) Part IV contains SGX's detailed comments; and

   (e) Part V contains SGX's conclusion to this submission.

5. Unless otherwise stated, references in this submission to section numbers are references to the corresponding sections in the Bill.

# II. SUMMARY OF MAJOR POINTS

6. SGX would like to thank MTI for the opportunity to give comments in this first round of public consultation. MTI has promised a second round of consultation. Our submission therefore deals with our key issues, assuming an opportunity to tackle less important issues in the next round.

7. SGX believes that MTI should exclude the securities and derivatives exchanges and clearing houses operated by SGX and its subsidiaries from sections 34 and 47 prohibitions of the Bill via an exclusion through the Third Schedule of the Bill.

8. We would like to propose a meeting with representatives from MTI and the relevant government authorities to formulate a regulatory solution to the issues we have raised.

9. SGX is asking for an exclusion from the Bill for the following reasons:

(i) Unique position and public function of SGX in Singapore

SGX occupies a unique position in the Singapore economy, and the exchanges and clearing houses play an important public function in Singapore. The efficiency and operation of these exchanges and clearing houses are vital for investment and economic growth in Singapore, and is heavily relied upon by both investors and businesses. The role played by SGX and its subsidiaries fulfil a vital public interest, and are therefore as crucial as other industries excluded from the Bill.

(ii) Natural monopoly characteristics

Securities and derivatives trading, and clearing and settlement have natural monopoly characteristics. This is due to economies of scale, network effects and novation. Thus, the market tendency is for such exchanges and clearing houses to integrate, as fragmentation is inefficient and not in the best interests of the market. This will be at odds with competition policy.

(iii) Highly technical knowledge and expertise required for effective regulation

In order to have efficient and effective regulation of the market, a high level of technical knowledge and expertise in the industry is required. Competition issues in the market which SGX and its subsidiaries operate cannot be determined without possessing an in-depth knowledge and appreciation of the unique characteristics of the industry. The Competition Commission is therefore going to be faced

with difficulty regulating the competition issues that will arise in relation to the activities of exchanges and clearing houses.

(iv) Inherent conflict between regulatory objectives and competition policy

There is an inherent conflict between regulatory objectives and competition policy in relation to the activities of exchanges and clearing houses. This is a universal and complex problem, as can be seen in the problems that have arisen in the other jurisdictions. The financial services regulator will be concerned with issues such as investor protection and confidence in the exchanges and clearing houses, whereas the competition regulator will be focused on competition issues such as barriers to entry. Finding the right balance between prudential regulation and competition is not easy. It usually requires specialist industry knowledge.

(v) Increase in the cost of regulatory compliance

Having two regulators, the Monetary Authority of Singapore ("***MAS***") and the Competition Commission, will increase the cost of regulatory compliance for SGX and its subsidiaries. This will put an unnecessary strain on our resources. In addition, this will also increase the cost of investment and trade in securities and derivatives in Singapore, as such costs will inevitably be passed on to consumers. On the other hand, excluding SGX and its subsidiaries from the Bill will keep the cost of regulatory compliance at the same level.

(vi) Tight regulation by MAS

The activities of the exchanges and clearing houses are already closely regulated by MAS. The SFA has put in place a tight regulatory framework part of which is already aimed at protecting consumers. The activities of such exchanges and clearing houses is just as, if not more, tightly regulated as compared to those industries which MTI has granted exclusions under the Third Schedule of the Bill. Therefore, SGX and its subsidiaries should be granted similar exclusions.

(vii) Potential allegations against clearing fees

Clearing fees are levied by CDP on investors based on the value of transactions. The nature and operation of clearing fees may give rise to challenges. Even if without merit (or we believe), there is cost and resource expense incurred. Please see paragraph 1 of Annex A (Confidential).

# III. STATEMENT OF INTEREST

10. Singapore Exchange Limited is Asia-Pacific's first demutualised and integrated securities and derivatives exchange.

11. SGX was demutualised on 1 December 1999, following the merger of two established and well-respected financial institutions – the Stock Exchange of Singapore and the Singapore International Monetary Exchange.

12. On 23 November 2000, SGX was listed via a public offer and a private placement. Listed on our bourse, our stock is a component of benchmark indices such as the MSCI Singapore Free Index and the Straits Times Index. At present, SGX and its subsidiaries operate a securities exchange, a derivatives exchange, and two clearing houses.

13. This submission represents the views of Singapore Exchange Limited and its subsidiaries.

# IV. DETAILED COMMENTS

14. SGX recognises that the Competition Bill is intended to introduce generic competition law into Singapore. Therefore, the Bill will be applicable to all 'undertakings', which will include SGX and its subsidiaries.

15. Exclusions are set out in the Third Schedule of the Bill. In the Third Schedule, services of a general economic nature, industries with sectoral competition regulation (such as the telecommunications, media, and electricity and gas industries), public transport services, banking clearing houses, etc., are excluded from section 34 and section 47 prohibitions.

16. SGX appreciates the necessity for many of these exclusions as they are due to public interest considerations such as national security, defence and other strategic or public policy interests. SGX notes that sectoral regulation in the telecommunications, media, and electricity and gas industries will remain without being affected by the Bill, as there are considerable technical matters affecting competition in these sectors and therefore sectoral regulators such as the Info-communications Development Authority of Singapore ("***IDA***") and the Media Development Authority of Singapore ("***MDA***") will take charge of competition issues arising in their respective sectors.

17. More could be done in the Bill to provide for similar exclusions for the securities and derivatives exchanges and clearing houses operated by SGX and its subsidiaries. Specifically, SGX is of the view that MTI should exclude the activities related to exchanges and clearing houses from section 34 and section 47 prohibitions. This stems from similar strategic and public policy considerations, namely, that these entities play a unique economic role in Singapore, and the application of generic competition law may result in a destabilising effect on the market.

18. Further, the experience in other jurisdictions demonstrates that there is an inherent tension between regulatory objectives and competition policies, and the policy objectives sought to be achieved by the two are often conflicting. In this respect, the following extract from the Supreme Court of the United States in the case of *Gordon v New York Stock Exchange, Inc., et al.*[1] is particularly instructive, and succinctly encapsulates the fundamental problem:

> "***If antitrust courts were to impose different standards or requirements [from that of the SEC], the exchanges might find themselves unable to proceed without violation of the mandate of the courts or of the SEC. Such different standards are likely to result because the sole aim of antitrust legislation is to protect competition, whereas the SEC must consider, in addition, the economic health of***

[1] **Gordon v New York Stock Exchange, Inc., et al.**
442 U.S. 659; 95 S. Ct. 2598; 45 L. Ed. 2d 463; 1975 U.S. LEXIS 115; 1975-1 Trade Cas. (CCH) P60, 367; Fed. Sec. L. Rep. (CCH) P95, 215.

> ***the investors, the exchanges, and the securities industry.*** Given the expertise of the SEC, the confidence the Congress has placed in the agency, and the active roles the SEC and Congress have taken, permitting courts throughout the country to conduct their own antitrust proceedings would conflict with the regulatory scheme authorised by Congress rather than supplement that scheme." [Emphasis added.]

19. The above judgment underscores the need for some form of immunity for exchanges and clearing houses from competition laws, and also underlines the difficult position of the businesses operated by SGX and its subsidiaries that will have to thread between two regulators with differing and conflicting policies.

20. Other jurisdictions have dealt with this problem either through a common law repeal of competition law or the introduction of new legislation. SGX feels that MTI is now in a position to address this problem, before the advent of competition law in Singapore, and should seriously consider granting SGX and its subsidiaries an express immunity from sections 34 and 47 prohibitions of the Bill by way of an exclusion through the Third Schedule. SGX believes that this would be a far neater arrangement and promotes greater certainty as opposed to an implied repeal via the common law.

***Unique position and public function of SGX in Singapore***

21. SGX occupies a unique position in the Singapore economy, and the infrastructure provided by SGX plays an important public function in Singapore. The formation of SGX is the result of a statutorily mandated merger between the Stock Exchange of Singapore and the Singapore International Monetary Exchange[2]. Both of these predecessors to SGX were respected and well-established financial institutions, and were vital to Singapore's economy and financial market. The merger arose out of the recommendations of a Committee appointed by MAS (the Committee on Governance of the Exchanges) which recommended, inter alia, that both exchanges position themselves as leading international exchanges for the trading of Asian products, and the trading of global products in Asia. Similarly, we feel that SGX also occupies a unique role in Singapore's financial market, as it is the infrastructure provider for the stock exchange, derivatives exchange and clearing houses in Singapore.

22. A securities and futures exchange is vital to Singapore, and indeed to most developed countries. A healthy and thriving securities and derivatives market is important to the economy. It is crucial for investment and economic growth in the country. Investors and businesses in Singapore rely heavily on SGX and its subsidiaries to conduct and operate its exchanges and clearing houses properly and efficiently. In the landmark case of *Silver v New York Stock Exchange*[3], the Supreme Court of the United States made the following

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2 Exchanges (Demutualisation and Merger) Act 1999 (Chapter 99B)

3 ***Silver, doing business as Municipal Securities Co., et al. v New York Stock Exchange*** 373 U.S. 341; 83 S. Ct. 1246; 10 L. Ed. 2d 389; 1963 U.S. LEXIS 2628

observation about stock exchanges and the vital role these exchanges play in the United States:

> "The need for statutory regulation of securities exchanges and the nature of the duty of self-regulation imposed by the Securities Exchange Act are properly understood in the context of a consideration of both the economic role played by exchanges and the historical setting of the Act. Stock exchanges perform an important function in the economic life of this country. They serve, first of all, an indispensable mechanism through which corporate securities can be bought and sold. To corporate enterprise such a market mechanism is a fundamental element in facilitating the successful marshalling of large aggregations of funds that would otherwise be extremely difficult to access. To the public the exchanges are an investment channel which promises ready convertibility of stock holdings into cash. The importance of these functions in dollar terms is vast…"

23. Given the importance of the public function played by SGX and its subsidiaries in Singapore's economy, the impact of the Bill on the exchanges and clearing houses should be addressed by MTI. In a sense, the role played by these exchanges and clearing houses is as vital as that of the other industries which are excluded from the Bill, such as public transport and the supply of piped potable water.

24. As MTI has already granted exclusions to industries such as the electricity and gas sectors and the cargo terminal operations industry in the Bill on the basis that these industries fulfil functions that are in the public interest, SGX submits that MTI should also extend such an exclusion to the businesses operated by SGX and its subsidiaries.

***Natural monopoly characteristics***

25. The trading of securities and derivatives through exchanges, together with clearing and settlement, are widely regarded to have natural monopoly characteristics. Fragmentation in the market is inefficient and is not in the best interests of the market. The natural monopoly characteristics of securities and derivatives trading, clearing and settlement, and its interaction with competition regulation have thus generated widespread debate in many jurisdictions.

26. For exchanges, the natural monopoly characteristics are due largely to economies of scale, technological advances, and the high fixed costs involved. In a recent article published on the subject, it is stated that "liquidity attracts liquidity and it is preferable to trade on the market where the majority of other investors have chosen to trade": Bagheri, *Competition and Integration among Stock Exchanges: The Dilemma of Conflicting Regulatory Objectives and Strategies* OJLS 2004.24(69).

27. In fact, there has been a historical trend towards the concentration of dominant market centres around the world. For example, there were 25 stock exchanges in the United States in 1935, but now there are only 10, amongst which the

New York Stock Exchange represents 95% of the trading volume. Similarly, in Europe, the national exchanges in France, the Netherlands, Belgium and Portugal and the integrated equity trading markets of Sweden, Finland, Denmark and Norway were merged to form Euronext.

28. The areas of clearing and settlement also share similar natural monopoly characteristics. Clearing houses are characterised by significant economies of scale and network effects, i.e. the more trades that are cleared by the same clearing house, the greater the potential for netting efficiencies. Efficient transacting and novation requires that securities, buyers and sellers link into the same clearing house. There are also economies of scale in risk management. Therefore, the natural monopoly characteristics produce a market structure in which there is a single clearing house. Any competition between clearing houses is likely to be transitory at best. SGX would like to draw MTI's attention to the following publications which discuss these aspects of clearing and settlement in substantial detail: see Niels, Barnes and van Dijk, *Unclear and Unsettled: The Debate on Competition in the Clearing and Settlement of Securities Trades* [2003] ECLR 634, and OXERA, *Review of the impact of the Financial Services and Markets Act 2000 on Competition*.

29. The natural monopoly characteristics of clearing and settlement is also well illustrated by the experience of the single clearing house in the United States, the National Securities Clearing Corporation (now part of the Depository Trust & Clearing Corporation). In the 1970s, there was not a single system, but a number of competing systems, with consumers having a choice of where to clear and settle. However, over time, all clearing businesses tipped towards this clearing house, which gradually took over the other US systems.

30. These natural monopoly characteristics of the business operated by SGX and its subsidiaries differentiate us from the banks. Unlike the banking industry, fragmenting the trading of securities and derivatives, clearing and settlement is not efficient and not in the interests of investors.

***Highly technical knowledge and expertise required for effective regulation***

31. We understand from Annex B of MTI's Consultation Paper to the Bill that one of the main reasons why selected industries, such as the electricity and gas sectors and the cargo terminal operations industry, are excluded from the Bill via the Third Schedule is that the sectoral regulators in these industries are better equipped to decide on competition issues. This is due to the considerable technical matters affecting competition in these sectors.

32. For example, MTI stated that dealing with competition issues in the electricity and gas industries would require specialist knowledge of how the electricity and gas industries work, and so the Energy Market Authority would be in a better position to deal with these issues. Similarly, MTI also stated that the operation of cargo terminal operations involves in-depth knowledge of the industry, and understanding of the complex relationship between different players along the value chain. It would be more appropriate for the Maritime and Port Authority of Singapore to decide competition issues that arise.

Therefore, these industries were excluded from the section 34 and section 47 prohibitions through the Third Schedule of the Bill.

33. SGX submits that the complexity and intricacies of the workings of the securities and derivatives exchanges and clearing houses and its operation in the financial services market makes it necessary for a similar exclusion to be extended to SGX and its subsidiaries. Competition issues in the market which SGX and its subsidiaries operate cannot be determined without having in-depth specialist knowledge and an appreciation of the unique characteristics of the industry.

34. For example, one unique characteristic of SGX is that it operates on a 'vertical silo' model, i.e. where the trading platform and clearing house are under common ownership and governance. This ensures efficiency and compatibility between the various layers, and such a structure should not be evaluated solely from a competition perspective without regard to the prudential concerns that a financial services regulator would have.

35. The highly technical nature of the market and the business means that the Competition Commission will not be suitably positioned to deal with the competition issues that arise from activities relating to exchanges and clearing houses operated by SGX and its subsidiaries.

36. The inability of pure competition regulators to efficiently regulate such activities was also recognised by the Banking Review of the United Kingdom in its independent investigative report, *Competition and Regulation in Financial Services: Striking the Right Balance*, where it stated that "the competition authority will not be fully equipped to understand the impact of changes along the regulatory dimension. The institution having the last word has to have the skills and incentives to understand both dimensions."

37. SGX feels that the activities concerning securities and derivatives exchanges and clearing houses are just as, if not more, complex and technical than those in the electricity and gas sectors, the cargo terminal operations industry, and other industries which have been granted exclusions from the Bill by MTI. If MTI deems it necessary to exclude the activities of such industries and sectors from the Bill due to the technical knowledge and expertise required for competent and effective regulation, we feel that similar exclusion should also be extended to the exchanges and clearing houses operated by SGX and its subsidiaries.

***Inherent conflict between regulatory objectives and competition policy***

38. At present, the competent authority regulating the activities of the securities and derivatives exchanges and clearing houses operated by SGX and its subsidiaries is MAS. Under the Securities and Futures Act ("SFA"), MAS is conferred with wide regulatory power in respect of such activities. For example, pursuant to section 9 of the SFA, a corporation must apply to MAS for approval if it wishes to operate as a securities or futures exchange in Singapore. Entry into the market is conditional upon MAS' approval. In addition, MAS closely regulates the content of the Business Rules for

exchanges and the Listing Rules for securities exchanges (sections 10 and 17 of the SFA) and the Business Rules of clearing houses (sections 52 and 59 of the SFA), and MAS can also review any disciplinary action taken by SGX and its subsidiaries against any of its members (sections 20 and 62 of the SFA). MAS also has the power to prohibit the trading in particular securities of any corporation in the securities market (section 23 of the SFA).

39. Further, similar to the other sectoral regulators such as IDA and MDA, MAS is given broad power under sections 21, 32 and 63 of the SFA to, if it thinks it necessary or expedient, issue directions to any securities or futures exchange, exchange holding company or clearing house for broad purposes such as "ensuring fair and orderly securities markets" or "in the interest of the public or section of the public or for the protection of investors". These directions issued by MAS are also expressly stated to be both of a general and specific nature. SGX and its subsidiaries are obliged to comply with such directions of MAS, or face possible sanctions in the event of non-compliance.

40. Thus, it can be seen that the activities and practices of exchanges and clearing houses operated by SGX and its subsidiaries in Singapore is already closely regulated and monitored by MAS. Parliament, through the SFA, has already put in place a tight regulatory framework, and this is mirrored in practice where SGX and its subsidiaries would closely consult MAS on matters.

41. The Bill, however, will introduce a new regulator in the form of the Competition Commission. In effect, exchange and competition regulation will co-exist. MAS will therefore defer all competition-related regulation to the Competition Commission. SGX submits that this will result in an undesirable state of affairs, as regulatory objectives and competition policies are conflicting.

42. The financial services regulator will, first and foremost, be concerned with issues such as investor protection, confidence in the local securities and futures exchanges and clearing houses, financial and economic stability, and Singapore's overall economic health. The Competition Commission, on the other hand, will be primarily concerned with competitiveness, barriers to market entry, and economic effect. Such objectives may not necessarily be consistent with the objectives of a securities regulator. The core problem in the regulation of the financial services provided by SGX is that necessary prudential or consumer regulation may, in some cases, have an appreciable anti-competitive effect. As SGX and its subsidiaries would have to ensure that it has to carry out its activities in compliance with the policies and objectives of both regulators, the potential for conflicting policies between the two regulators is a worrying one for SGX.

43. SGX would also like to point out to MTI that the experience in the United States and United Kingdom also demonstrates the tension between these conflicting regulatory objectives, and highlights the problems that could arise from such conflict.

United States experience

44. In *Gordon v New York Stock Exchange, Inc., et al.*[4], the Supreme Court of the United States held that with respect to the fixing of commission rates by the New York Stock Exchange, there is an implied repeal of antitrust laws. This is because the Securities and Exchange Commission (the "***SEC***"), which is the regulator for the New York Stock Exchange, had direct regulatory power over the fixing of such rates and has taken an active role in review of proposed rate changes over the last 15 years. The Court stated that "to deny antitrust immunity with respect to commission rates would be to ***subject the exchanges and their members to conflicting standards***". [Emphasis added.] The Court had to ultimately imply a repeal of antitrust laws in order to circumvent the express wording of United States antitrust legislation. The case of *Gordon* clearly illustrates the necessity for, and recognition by, the Courts for some form of immunity to reflect the practical realities in the securities market.

45. *Gordon* was approved by the United States Court of Appeals for the Fifth Circuit in *Harding v American Stock Exchange, Inc.*[5]. In *Harding*, the applicant, who was a stockholder of a particular company, brought the suit against the American Stock Exchange for alleged violation of antitrust laws. The applicant challenged the American Stock Exchange's suspension of the trading in that company and its application to the SEC for delisting of the company's stock. The Court held that the regulatory scheme and the SEC's order approving the delisting leads to the conclusion that the American Stock Exchange's alleged violations are outside the ambit of antitrust laws. This is because immunity from antitrust laws "is necessary to make the Exchange Act viable". As the United States Exchange Act had provided that any security may be withdrawn from listing "upon such terms as the [SEC] may deem necessary to impose for the protection of investors", an implied repeal of antitrust laws was deemed necessary in this instance to ensure the viability of the Act.

46. The conflict between regulatory objectives and competition was again examined in the more recent case of *In re: Stock Exchanges Options Trading Antitrust Litigation Lynn S. Miller*[6] (decided on 9 January 2003), where the United States Court of Appeals for the Second Circuit stated that immunity from antitrust laws "turns on whether the antitrust laws conflict with an overall regulatory scheme that empowers the agency to allow conduct that the antitrust laws would prohibit". On the facts of that case, the Court found that the SEC has ample statutory authority, which it has repeatedly exercised, to regulate the listing and trading of equity options, and on this basis, concluded

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4 ***Gordon v New York Stock Exchange, Inc., et al***
442 U.S. 659; 95 S. Ct. 2598; 45 L. Ed. 2d 463; 1975 U.S. LEXIS 115; 1975-1 Trade Cas. (CCH) P60, 367; Fed. Sec. L. Rep. (CCH) P95, 215.

5 **Henry W. Harding, an owner of 330,500 share of common stock of Siboney Corporation, et al. v American Stock Exchange, Inc.**
527 F.2d 1366; 1976 U.S. App. LEXIS 12500; 1976-1 Trade Cas. (CCH) P60, 761; Fed. Sec. L. Rep. (CCH) P95, 461.

6 **In re Stock Exchanges Options Trading Antitrust Legislation Lynn S. Miller et al.**
317 F.3d 134; 2003 U.S> App. LEXIS 277; 2003-1 Trade Cas. (CCH) P73, 927; 50 Collier Bankr. Cas. 2d (MB) 1346.

that the US Exchange Act impliedly immunises the defendant stock exchanges against liability under antitrust laws.

47. These United States cases plainly demonstrate that conflict is inherent in the relationship between prudential regulation and competition policies, and that Courts have recognised this conflict by allowing the stock exchanges immunity from antitrust laws by way of an implied repeal. The need for an implied repeal arose due to the lack of an express exclusion in the United States legislation, but was deemed necessary so as to avoid a conflict between antitrust laws and regulatory objectives. However, as competition law has yet to be formally introduced and implemented in Singapore, MTI is in a unique position to deal with this directly.

United Kingdom experience

48. Immunity from competition law for exchanges and clearing houses is not restricted to the United States. In the United Kingdom, recognised investment exchanges, such as the London Stock Exchange, and recognised clearing houses are expressly excluded from the prohibitions of the UK Competition Act 1998. Both the Chapter I (Agreements) and Chapter II (Abuse of Dominant Position) prohibitions do not apply to recognised bodies such as the London Stock Exchange. Specifically, section 311 of the UK Financial Services and Markets Act 2000 states that the Chapter I prohibition does not apply to, inter alia, the practices of recognised investment exchanges and clearing houses and agreements entered into by such recognised bodies. Section 312 of the same Act provides that the Chapter II prohibition does not apply to, inter alia, the practices and conduct of such exchanges and clearing houses.

49. In essence, recognised investment exchanges and clearing houses in the UK such as the London Stock Exchange are excluded from the UK Competition Act 1998 in a manner similar to that envisaged by the Third Schedule of the Bill. SGX is of the view that MTI should therefore consider a similar exclusion for the exchanges and clearing houses operated by SGX and its subsidiaries in the Bill, especially since the Bill is substantially modelled after the UK Competition Act 1998.

50. To ensure some measure of competition scrutiny, the UK model provides that the Office of Fair Trading (the "***OFT***") will play a 'watchdog' role to ensure that competition is still maintained. The financial regulator in the UK is the Financial Services Authority (the "***FSA***"). However, while the FSA is the main regulator for the exchanges and clearing houses, under Part X, Chapter III of the UK Financial Services and Markets Act 2000, the OFT has a statutory obligation to keep the FSA's rules and practices under competition scrutiny, i.e. to assess whether there is any "significant adverse effect on competition". Part XVIII, Chapter II of the UK Financial Services and Markets Act 2000 also contains similar competition scrutiny provisions in relation to recognised investment exchanges and clearing houses, where it states that the OFT will "keep under review the regulatory provisions and practices" of these exchanges and clearing houses. Should the OFT consider certain activities to have a significantly adverse effect on competition in the

UK, the OFT will submit a report to the UK Competition Commission for its consideration.

51. This arrangement ensures that while there is still competition scrutiny, some measure of protection is afforded to exchanges and clearing houses as they are excluded from the prohibitions of the UK Competition Act 1998.

52. The financial services regulator for the UK has the jurisdiction to take into account competition law matters in the exercise of its regulatory functions and duties. Section 2(3)(f) of the UK Financial Services and Markets Act 2000 states that, in the discharge of its general functions, the FSA must have regard to "the need to minimise the adverse effects on competition that may arise from anything done in the discharge of those functions".

53. This model could successfully be applied here. SGX submits that the problem of conflict must be met by MTI head on, and should certainly be dealt with before the implementation of competition law in Singapore. From the experiences of the mature competition jurisdictions with established financial markets such as the United States and the United Kingdom, the conflict between regulatory objectives and competition policies is a complex and universal problem, and it suggests that some form of immunity and safeguard should be afforded to exchanges and clearing houses in order to strike the right regulatory balance. In addition, it appears that the more successful balance is struck when the competition analysis is part of the regulatory process.

54. In this respect, SGX is of the view that the exclusion of securities and derivatives exchanges and clearing houses from sections 34 and 47 prohibitions of the Bill by way of an amendment of the Third Schedule of the Bill will be the most effective means of reducing the potential for such regulatory conflict. Certainly, SGX will be happy to discuss this further with MTI and the relevant government authorities to work out feasible solutions if required.

***Increase in the cost of regulatory compliance***

55. While SGX has serious concerns regarding the potential problems that will arise from the conflict between regulatory objectives and competition policy, we believe that the most immediate detrimental effect of competition law on the financial services market will be the increase in the cost of regulatory compliance for SGX and its subsidiaries.

56. MAS is currently the sole regulator of the businesses and activities of SGX and its subsidiaries. The Bill, however, will introduce an additional regulator to regulate such activities. There is no doubt that SGX and its subsidiaries will have to incur substantive costs in an effort to ensure regulatory compliance.

57. The cost of ensuring regulatory compliance with a single regulator in the market is already significant. The increase in the cost of having to comply with competition regulation, as well as regulation by MAS, will put an

additional strain on the resources of SGX and its subsidiaries, and inevitably lead to wastage. Having two regulators is therefore inefficient.

58. More importantly, the increase in the cost of regulatory compliance will ultimately be borne by consumers, as SGX and its subsidiaries will inevitably have to pass on these costs. This will lead to an increase in the cost of investment and securities and derivatives trading, and will be detrimental to businesses and commerce in Singapore and therefore to the Singapore economy.

59. Finally, this increase in the cost of regulatory compliance may, ironically, dampen competition in the markets, as the barriers to entry are pushed higher. Already, there are substantial barriers to entry for a party who wishes to operate an exchange, due to the limited market size in Singapore and the high fixed costs involved. Increasing costs related to regulatory compliance will only raise these barriers to entry, and cannot be beneficial for the financial markets in Singapore.

60. Therefore, SGX is not in favour of having two separate regulators as this would unnecessarily increase the cost of regulatory compliance in the securities industry, and would recommend to MTI that SGX and its subsidiaries be excluded from the Bill under the Third Schedule.

***Tight regulation by MAS***

61. SGX also feels that an exclusion of securities and derivatives trading, clearing and settlement from the Bill is warranted by the fact that there is already tight regulation by MAS over such activities and businesses of SGX and its subsidiaries.

62. MTI should consider that the market in which SGX and its subsidiaries operate is one of the most tightly regulated markets in Singapore. In fact, SGX submits that regulation by MAS is just as, if not more, stringent when compared to the sectoral regulators in those industries which MTI has deemed necessary to exclude from the Bill. SGX and its subsidiaries closely consult MAS on many matters relating to our activities in the market, and an inspection of the SFA will reveal that a tight regulatory framework has already been put in place by Parliament.

63. Therefore, given the pervasiveness of the regulatory scheme, SGX urges MTI to seriously consider excluding securities and derivatives exchanges and clearing houses managed by SGX and its subsidiaries from the Bill.

***Potential allegations against clearing fees***

64. The final point we wish to highlight to MTI is the potential problems with clearing fees should the Bill be applicable to SGX and its subsidiaries. In the equities market, the clearing fee is essentially a fee which CDP, a wholly-owned subsidiary of SGX, levies on investors who trade in securities. The clearing fee is pegged to the value of trade activity. Therefore, the more an

investor trades, the more clearing fee the investor has to pay to CDP (up to a maximum of $200). Please also see paragraph 2 of Annex A.

65. If the Bill applies, we anticipate that an allegation of predatory pricing may be made against CDP. The maintenance of securities accounts in the Central Depository is free.

66. This may give rise to an allegation that SGX infringed section 47 as it can be alleged to be "predatory behaviour towards competitors". Only investors who trade beyond a certain amount will cover the cost of maintaining their securities accounts in the Central Depository.

67. Although the argument is without merit, and we appreciate that pricing below marginal cost or average variable cost does not necessarily amount to predatory pricing, SGX is concerned that such an allegation could potentially be made against CDP. This would lead to an extremely unsatisfactory state of affairs for SGX.

68. Secondly, there is also a possible allegation that CDP is infringing section 47 by engaging in cross-subsidising.

69. Again, this is without merit but the Bill offers no protection to SGX in this regard.

70. Thirdly, the Bill also give rise to an (unmeritorious) allegation of mandatory bundling by CDP or SGX, as investors who maintain their securities accounts with CDP have to trade, settle and clear their transactions within the infrastructure provided by SGX and its subsidiaries.

71. There is at least one case in the United States where charges fixed by stock exchanges were held to be immune from competition law. In *Gordon v New York Stock Exchange, Inc., et al.*[7], investors challenged the New York Stock Exchange rules by which stockbrokers fixed their commission charges. Under section 19(b)(9) of the United States Securities Exchange Act, the SEC could alter or supplement exchange rules relating to the "fixing of reasonable rates of commission". The Supreme Court of the United States held that this regulatory authority of the SEC, coupled with the SEC's actual record of vigorous scrutiny over commissions, immunised the challenged behaviour from United States antitrust laws. The Supreme Court added that antitrust immunity was therefore necessary to make the United States Securities Exchange Act work, and lest antitrust courts impose on the stock exchanges a requirement different from that imposed by the SEC pursuant to its express statutory power to supervise and set commission rates.

72. The ruling by the Court is a sensible one, as to declare the fixing of commission charges a violation of antitrust laws would negate the very purpose of securities regulation, and also put the stock exchanges in an untenable position. SGX is extremely concerned with the potential for

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[7] ***Gordon v New York Stock Exchange, Inc., et al***
442 U.S. 659; 95 S. Ct. 2598; 45 L. Ed. 2d 463; 1975 U.S. LEXIS 115; 1975-1 Trade Cas. (CCH) P60, 367; Fed. Sec. L. Rep. (CCH) P95, 215.

allegations of violation of competition law with regards to the clearing fee once the Bill is enacted. If SGX or any of its subsidiaries is found to be in violation of the provision of the Bill by the Competition Commission as a result of its clearing fees, this may call into question the viability of the regulatory framework in the securities industry as SGX would in effect be acting anti-competitively as a result of regulation by MAS. This would result in an undesirable state of affairs, and should be addressed by MTI in the Bill.

73. Therefore, by analogy, SGX strongly urges MTI to exclude the activities of SGX and its subsidiaries from the Bill, and immunise SGX and its subsidiaries from allegations of anti-competitive behaviour as a result of CDP's clearing fees and free custody of securities accounts held by the Central Depository.

# V. CONCLUSION

84. SGX welcomes the opportunity to participate in this round of the public consultation exercise.

85. SGX hopes that MTI will seriously consider SGX's submissions on the Bill. We will be happy to answer any queries MTI may have arising from this first round of public consultation.

86. SGX looks forward to future involvement in the public consultation process.