

## Chapter 8

# E-Governance in the Financial Capital Markets: The Canadian Capital Market Regulatory Environment

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### ABSTRACT

*Studies of corporate governance in the capital markets area have focused on the mechanisms and structures of governance and less on the medium through which it is accomplished. This chapter examines the use of information and communications technologies (ICTs) as a medium to enhance governance in the capital markets, focusing in particular on the Canadian capital market. Parallels are drawn between the e-governance issues faced by governments and the capital markets. The chapter concludes with a discussion of future directions for e-governance in the capital markets.*

### INTRODUCTION

Academics, professionals, investors and citizens have become increasingly interested in the governance of the organizations with which they interact on a daily basis. In addition, over the past twenty years, advances in information and communica-

tions technologies (ICTs) have improved the ability of these organizations to provide relevant information to interested parties. As a result of the increased interest in governance and the increased availability of information, discussions of good or poor governance can be found everywhere, from the local, national and international media to academic journals and conferences.

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Academics have focused most of their efforts on the study of governance in corporations and government. In particular, an extensive literature on the use of ICTs as a medium to enhance governance in local, regional and national governments, also known as electronic governance or e-governance, has developed. The ICTs utilized by governments were often adopted from the corporate environment and subsequently used by governments to improve transparency and responsiveness (Perez, Bolivar and Hernandez, 2008). Interestingly, the corporate governance literature in accounting and finance has focused on the mechanisms and structures of governance (Durisin and Puzone, 2009) and less on the medium through which it is accomplished. This chapter will examine the use of ICTs as a medium to enhance governance in the capital markets, focusing in particular on the Canadian capital market.

The remainder of the chapter is organized as follows. First, the Canadian capital markets are briefly described. Second, governance practices generally and e-governance practices in particular are reviewed for the Canadian capital markets. Third, information from relevant studies of governance applicable to the Canadian capital markets are summarized and issues associated with the use of electronic governance are identified. Fourth, parallels in e-governance in the financial capital markets and in governments are identified. Finally, future directions of e-governance in the Canadian capital markets are discussed.

## **THE CANADIAN CAPITAL MARKETS AND THE REGULATORY ENVIRONMENT**

Canada is characterized by well-developed capital markets as evidenced by the fact that the market capitalization of exchange-listed issuers is high relative to Canada's GDP<sup>1</sup> (Nicholls, 2006). The capital markets consist of a number of individual markets, the most well known are the markets for

equities and fixed-income. In Canada, most equities are traded on organized exchanges (i.e., auction markets), primarily the Toronto Stock Exchange (TSX) and the TSX Venture Exchange<sup>2</sup>. In contrast, most fixed-income products are traded in dealer or "over-the-counter" (OTC) markets. According to the World Federation of Exchanges, the TMX Group, with a domestic market capitalization of \$1.7 trillion in 2009, was the eighth largest stock market in the world.

The regulatory system for the capital markets in Canada is ranked as one of the best in the world. In 2009, the Organization for Economic Co-operation and Development (OECD) ranked Canada fifth in the world in investor protection. In Canada, the capital markets, and the financial industry more generally, are characterized by extensive use of technology, in fact, much of their business is conducted electronically. Further, most of the information required by regulators (to be distributed to the public or provided to the regulators) is disclosed electronically. These factors make Canada a particularly good example to use to examine the use of electronic governance.

The Canadian capital markets have two other distinct features. First, companies who are traded on the stock market must either comply with a set of recommended best practices for corporate governance or, alternatively, explain how they will achieve the same governance objective in a different manner (i.e., "comply or explain"). This principles-based approach to governance recognizes that the costs and benefits of the governance requirements are likely to be different for small firms as compared to large firms. This feature means that there should be more variability in governance practices than under a rules-based approach to corporate governance. A second feature of the Canadian capital markets is that it does not have a national regulator<sup>3</sup>. In Canada, the regulation of the securities business has been assumed by the provinces. In contrast to the United States (which has the Securities and Exchange Commission or SEC), no federal

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