INTERCONTINENTAL EXCHANGE/TRAYPORT MERGER INQUIRY

Summary of hearing with Griffin Markets Group Limited on 26 May 2016

Background

1. Griffin Markets Group Limited and its subsidiaries (Griffin) was a broker operating a hybrid electronic/voice over the counter (OTC) trading platform. Griffin stated that it used Trayport as a software provider for its platform for dealing in energy markets.

Licence and Service Agreement with ICE

2. Griffin stated that it was set up in September 2011 as an alternative energy broker that was more transparent and used different technology to challenge the position of Trayport. Griffin said that it partnered with ICE under a [✂] Licence and Services Agreement (LSA) with a plan to use ICE's technology in order to set up an alternative trading platform on the ICE matching engine accessed through the WebICE front-end (the equivalent of the Trayport front-end screen). Griffin intended to try to migrate liquidity away from the Trayport platform onto the Griffin/ICE platform in many of the energy markets. [✂].

3. Griffin said that for its back-end software it used ICE legacy technology, the ICE matching engine, which traders could access through the WebICE front-end. ICE hosted the service and carried out the administration on instruments and users, whilst Griffin operated the marketplace. However, due to a lack of aggregation with the Trayport system, Griffin's marketplace was a second or third screen for traders behind Trayport and ICE futures. So a UK gas trader would have the relevant screen open in WebICE to look at the ICE futures National Balancing Point (NBP) market alongside the Trayport screen which showed the OTC NBP market. Griffin's market was another tab on the WebICE screen which the trader could open. Griffin needed to migrate liquidity quickly to persuade a trader to open its tab.

4. Griffin said that ICE had to approve any third party systems wanting to connect to Griffin's platform and had a right of veto but Griffin managed to connect a small number of third party systems such as Exxeta AG (an independent software vendor (WASV) - which was also connected to Trayport's Trading Gateway). Griffin planned to use a network of third party systems to produce an aggregated view of the market to rival Trayport. Griffin

aimed to offer a lower cost/higher integrity service. Traders who switched to Griffin would be switching from Trayport's back-end to ICE's matching engine. Griffin's strategy was to have a more electronic solution, rather than requiring large teams of brokers, which would enable it to pass on cost savings as part of its fee structure. It hoped that a competitive platform with lower costs would be enough to shift liquidity.

5. Griffin said that it failed to migrate liquidity from the Trayport platform. One of the primary reasons for the failure of the system was the lack of aggregation available on the ICE platform. Griffin explained that it terminated the LSA with ICE in 2014 and switched to Trayport. Since that point Griffin's broker operation had conducted significantly higher levels of business as a result of being on Trayport. When Griffin was on ICE it had the same fee structure, the same business model, the same marketers, the only difference was that they were on a different technology platform and that platform had no aggregation.

6. Griffin said that it was theoretically possible for firms to switch away from Trayport's infrastructure. However, in the markets where Trayport was strong, Griffin's experience was that it was not a practical option as it was unlikely that there would be any aggregation of products from different venues in the new platform without wholesale migration. Griffin said that without aggregation, traders would need multiple screens – one for each marketplace - containing the information they needed to make trading decisions but that traders wanted to be able to see the market in one aggregated stack. Griffin's ICE offering was outside of that aggregated screen and it was, therefore, onerous and inefficient for traders who had to look at more than one screen to try to work out the best bid, or the best offer.

7. Griffin said that although it had been able to connect a large number of counterparties to its ICE platform, Griffin thought that its experience showed that aggregation was a barrier that could not be cleared. It stated that the difficulties in shifting liquidity in these markets arose due to the large number of counterparties. Liquidity in the markets was not split between individual broker screens but was consolidated by Trayport, into one liquidity pool. If a broker were to change its back-end from Trayport's, then it would be unlikely to be able to aggregate its prices into the Trading Gateway; traders would have to view this market in isolation.

8. Griffin also said that trading counterparties would face a large number of issues in switching to a new technology. It would involve a huge amount of investment and analysis, and it would be a big challenge to persuade each major counterparty to shift to an alternative technology simultaneously.

9. Griffin said that it played a key role in getting the WebICE platform onto the desktop of traders in Europe and migrating liquidity to the ICE platform. ICE also benefited because counterparties who were not already using WebICE had to carry out trade capture work so that trade information would flow through into their Energy Trade Risk Management (ETRM) systems. This meant that these counterparties could also capture trades executed on the ICE futures exchange which they could not do previously which was an obvious advantage for ICE.

10. Griffin stated that neither CME nor NASDAQ were better placed to offer an alternative platform in 2011. This situation had not changed since.

11. [✂].

Switching between OTC and exchange trading

12. Griffin stated that the fundamental difference between futures markets and OTC bilateral markets, was that on a futures exchange (with the requisite permissions/access) you could trade any price on that screen. In a bilateral marketplace you would have master agreements with multiple counterparties and if a counterparty placed a trade on the screen you could only trade with them if you had a master agreement with them and good credit. If you did not then that order was untradeable for you. In this context, it stated that futures platforms would require significant investment to be converted to operate as OTC bilateral platforms.

13. [✂].

14. Griffin stated that it considered that the movement from OTC into futures was a real possibility at the time. However, the regulatory landscape had changed since that point. Griffin noted that it now considered that there was more of a pathway for the OTC markets to thrive.

15. Griffin indicated that financial counterparties would be most likely to switch between OTC and exchange trading, as they were not concerned whether they were trading financial instruments since they were already regulated as financial entities.

Griffin post-LSA with ICE

16. Griffin negotiated a licence agreement with Trayport under which Griffin switched to the Trayport Broker Trading System (BTS) on 1 July 2014. Griffin indicated that it had enjoyed more success following termination of its LSA with ICE.

17. Griffin stated that the power of Trayport was demonstrated by the fact that it took 12 months to launch its offering with ICE, whereas it took less than a month to launch its offering with Trayport. It also stated that it was the number one broker in the title transfer facility (TTF) front month market on its first day. Griffin, as a broker, had not got close to this volume of activity when it was on ICE.

18. Griffin stated that there was no charge for traders to access the ICE front-end, and the Griffin marketplace. However, Griffin stated that there were some significant functionality gaps between the OTC ICE platform which Griffin was using and Trayport's which presented Griffin with difficulty in trying to migrate liquidity. It stated that while ICE was better at high volume markets, it did not address the needs of a European energy trader in the OTC bilateral markets. Griffin stated that one of the hurdles that it faced was that, simultaneously, ICE was migrating the London International and Financial Futures and Options Exchange (LIFFE) onto WebICE following ICE's acquisition of NYSE. This meant that Griffin faced difficulties in focusing ICE on providing Griffin with the functionality it needed to succeed.

Griffin on Trayport

19. Griffin stated that Trayport's software had been in the marketplace for coming up to 20 years. Traders had invested significant levels of effort into building in decision making tools, compliance systems and similar functionality integrated into Trayport's system.

20. [✂].

21. [✂].

22. Griffin stated that the main value of Trayport, in addition to the aggregation that it had achieved, was the closed access programming interface (API) strategy that it was operating due to its control of both the back-end and front-end systems. With the closed API in operation, there was only room for one aggregating platform where liquidity gathered.

23. Griffin explained that, in the context of the current regulatory environment, some counterparties would be very keen to trade in the OTC market as much as possible. This was because they did not want to trade financial instruments, which were caught by regulatory requirements under MiFID. Companies trading financial instruments could be required to be regulated like a bank; this would be costly for come companies.

24. Griffin stated that a key future development was a credit API, a way of electronically importing credit onto platforms. This would be a particularly useful feature, which would make the underlying data for the bilateral trading process more accurate by removing manually keyed errors. Griffin said that it was concerned that such developments currently being considered by Trayport would be halted by ICE because improving the efficiency of the OTC market could damage liquidity on ICE's futures exchange.

Clearing

25. Griffin stated that it preferred not to use Trayport's hosted clearing link because it had more control over trades coming through its back-office system. Instead, Griffin preferred to use its own direct links to clearing houses.

26. [✂].

27. [✂].

28. Griffin stated that it operated its OTC platforms with discretion. This was important from a regulatory perspective as trades could be carried out in a way that they did not become financial instruments. If the ability to act as a discretionary platform was taken away, by, for example, losing control over the processing of a trade, then this could jeopardise brokers' ability to process non-financial instruments in the energy markets.

Griffin on data transfer

29. Griffin stated that execution and order data sat on Griffin's broker system, Griffin owned that data, but was constrained as to what it could do with the data by the Trayport agreement. For example, Trayport restricted Griffin from selling its data to a third party in a way that enabled the third party to aggregate the data with full market depth, in real time. Trayport believed this would compete with the Trading Gateway. Griffin stated that even though Trayport did not own its data, it effectively sold Griffin's data to counterparties by selling view-only screens through the trading gateway.

30. Griffin stated that following the merger ICE could have access to Griffin's data, which contained confidential information on Griffin's customers. Contractually, ICE was prevented from accessing Trayport's data but Griffin remained concerned that sufficient Chinese walls were put in place to prevent ICE from accessing this data post-merger.

Exchange and OTC markets

31. Griffin stated that there was a fundamental difference between trades executed on exchange and OTC. Trades on exchange were anonymous and cleared, they did not have the counterparty risk associated with OTC trades as a central clearing house was used. OTC markets were predominantly bilateral. So, if counterparty A was selling gas to counterparty B, A and B needed to know who they had dealt with because A needed to deliver gas to B and B needed to pay A. In the cleared market it was still a physical product, but A sold the gas to the clearing house and the clearing house sold the gas to company B.

32. Griffin stated that shifting volumes of OTC trading to exchange trading would require traders to move from not clearing their trades to clearing them. In relation to whether clearing would require additional costs and whether switching to exchange trading would be desirable, Griffin indicated that it would depend on a variety of factors. It emphasised that the identity of the counterparty would be particularly determinative.

33. Griffin stated that it believed that ICE's fee structure was set according to where other exchanges, such as CME and EEX, set their execution and clearing fees as they were ICE's direct competitors. Griffin stated that traders paid a different price for registering trades via an exchange, or through a broker. ICE competed on price to drive liquidity to WebICE.

34. Griffin considered its own fee structure to be constrained by other brokers' fees rather than exchanges, as the decision to trade through an exchange or an OTC broker was not driven by price alone. It considered that trading through an exchange was partly driven by clearing anonymity, whereas trading through a broker was partly driven by a desire to trade bilaterally. However, it stated that the merged entity could drive liquidity to the exchange platforms by either changing technology or increasing price significantly.

35. Nevertheless, Griffin stated that it competed directly with exchanges on execution. Traders faced a choice of whether to execute through an exchange, or to execute through a broker. In particular, financial counterparties such as banks or investment firms were more likely to switch between OTC and exchange trading as they were not so bothered about whether they were trading financial instruments or whether they were trading outside of MiFID, as they were already regulated as financial entities. These businesses were likely to be more concerned with trading in the market where liquidity was.

Griffin on competition between ICE and Trayport

36. Griffin stated that it did not believe that there was competition between ICE and Trayport for the provision of technology services to OTC brokers. Griffin stated that there was currently no one who provided an alternative software to enable a technology platform to launch in competition to Trayport.

37. Griffin stated that ICE and Trayport competed in terms of offering access services to traders, for example, as a trader you could access ICE's futures markets through WebICE or through Trayport. Griffin stated that traders could access Trayport and trade on other venues supported by Trayport and which provided competing products to ICE, particularly gas and power. As a trader, if you wanted to trade ICE futures, you could choose from a large number of front-ends. If a trader wanted to trade on Trayport through a broker, such as Griffin, then the trader had to have Trayport's Trading Gateway if they wanted to aggregate those markets.

Post-merger effects

38. [✂].

39. [✂].

40. [✂].

41. [✂].

Closing statements

42. [✂].

43. Griffin stated that the opening of Trayport's API and the fundamental change this would bring to the dynamic of the market would introduce the competition that the market needed.