Greg Bonne
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Competition and Markets Authority
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By email

23 September 2016

Dear Mr Bonne

EXCHANGE C'S RESPONSE TO ICE'S REMEDIES PROPOSAL DATED 9 SEPTEMBER 2016

The CMA published ICE's remedies proposal on 15 September and invited EXCHANGE C, along with other third parties, to submit a response should our views thus far expressed be altered by the current proposal. EXCHANGE C welcomes the opportunity to comment on ICE's remedy proposal and the continued engagement by the CMA with third parties in its merger inquiry.

As outlined in our previous submission on the CMA's Remedies Notice, EXCHANGE C strongly believes that full divestiture is the most effective way to remedy the competition concerns identified by the CMA. A successful full divestiture will maintain the competitive structure of the market and thus deal with the SLC more directly and comprehensively than any possible package of behavioural remedies.

We do not believe that ICE's current remedies proposal adequately addresses the SLC outlined in the CMA's Provisional Findings. The proposal does not come close to sufficiently addressing the circumvention and specification risks outlined in detail in our response to the CMA's Remedies Notice ('previous remedies submission'). The proposed monitoring and enforcement of the remedies would without doubt be utterly inadequate and there is no FRAND provision applying to existing contracts, however long these might be extended, only to new contracts.

Much of our reasoning outlining why the currently proposed remedies would be completely ineffectual is already outlined in detail in our previous remedies submission. We do not repeat these points here but instead highlight a number of concerns specific to the current proposal. We also take the opportunity to make some high level comments relating to ICE's substantive response to the Provisional Findings, which misrepresents how competition works in the sector and selectively addresses some but not all of the CMA's reasons with the effect of misrepresenting the impact of the merger on competition.

ICE's Current Remedies Proposal

ICE has sought to address the SLC by offering to: extend existing licenses; maintain similar or improved performance, and dedicate equivalent resources to the development, of Trayport; impose confidentiality firewalls; and operate Trayport semi-autonomously from ICE. No provisions are made for the opening of Trayport's API. These are addressed in turn below.

Before this, EXCHANGE C feels it important to challenge ICE's claim that concerns and complaints with the merger have been made only by self-interested competitors seeking to damage ICE. First, this is self-evidently false as trading customers also have significant concerns with the merger and indeed the most prominent European trader association body has raised concerns on behalf of trading companies. This is

important as trade bodies can express collective views of their representatives, particularly where traders themselves may be especially concerned about ensuring confidentiality or where harm may be very significant in total but the effect on each individual customer may be more disparate. Also some companies do not have the legal means to directly comment on this case and likely preferred to rely on their professional association. Second, EXCHANGE C has made clear in its submissions that it has no issue with fair competition. Our submissions have not sought to penalise ICE or weaken its competitive position but only to ensure that ICE cannot use its acquisition of such an important factor in the competitive strength of competing venues and clearing houses as Trayport to unfairly gain advantage, leading to competitive harm.

No provisions for opening the APIs

EXCHANGE C believes opening the Trayport APIs is a necessary condition for an effective remedies package short of divestiture. If Trayport back-ends were to have an open API this would allow different ISVs to connect to Trayport and reduce the market dependency on Trayport for brokers, exchanges and traders, particularly important in the event of misuse of Trading Gateway by ICE post-merger. Similarly, an open API to the broker back-ends will ensure fair competition to the Clearing Link and an open API for Trading Gateway will ensure that no platform or product could be excluded from the Trayport front-end. Details of the necessity of opening the APIs to ensure an effective remedies package short of divestiture is outlined in detail in our previous remedies submission. In summary, the lack of open API has been the key reason underpinning Trayport´s closed network and thus the reason those reliant on Trayport are unable to develop alternatives. The ability for ICE to leverage this closed network post-merger is at the core of many of the issues raised by the merger; the absence of a provision opening the API in the current remedies package is therefore a key concern.

Instead, in its current proposal, ICE specifies that:

> '*4. Trayport may not include an exclusivity term that prohibits the customer from using alternative software products sold by companies other than Trayport*.'

This does not resolve the issues relating to Trayport's closed API at all. First of all, the Trayport contracts that we are aware of already do not have exclusivity terms. Venues can use other back-ends (most brokers use for example other back-ends for other asset classes) and traders use different front-ends to also access other asset class. The concerns are not related to exclusivity. The provision suggested by ICE may enable venues and traders to work with alternative ISVs but without a connection to Trayport back-ends, and an open API under reasonable price and technical conditions, such arrangements are meaningless. An appropriate remedy must include provisions that allow customers to fully use all aspects of Trayport products, for example, open access to and usage of the BTS/ETS for an ISV or any STP developer or ensure that new or existing venues cannot be refused listing (including for specific products and instruments) on Trading Gateway.

No FRAND terms are proposed for existing license-holders

The proposal states that Trayport will license, improve and support its products on a venue-neutral basis but no FRAND terms are proposed for basic day-to-day operations of Trayport for those *under an existing contract*. ICE proposes honouring the terms of existing licenses (without monitoring of whether this is the case, which is considered further below). This is clearly not sufficient to prevent an SLC from arising. Indeed, alongside the absence of any reasonable monitoring, these aspects of the proposal are equivalent to allowing the merger to proceed unconditionally. For example, there is nothing in the current remedies proposal that would prevent ICE from delaying the price discovery of a competing venue and nothing to ensure venue-neutral prioritisation of customer requests.

The criteria for being venue-neutral and not giving unfair competitive advantage to ICE would have to be specified in considerable detail. EXCHANGE C has significant concerns over the extent to which this could be done in a way that prevents the SLC. As EXCHANGE C has mentioned in its previous remedies submission, any obligations stipulated by the CMA would struggle to be sufficiently comprehensive that ICE could not circumvent these specific obligations by foreclosing competitors through other means.

Trading venues are active in a large number of products with different characteristics with each trading venue operating under different technical and commercial terms with Trayport, reflecting also the maturity and level of development of the market under consideration. Capturing all these situations in a FRAND framework would be very challenging and new situations appear all the time due to the constantly changing nature of the European energy business.

Monitoring and enforcement provisions are wholly inadequate

One of the most striking aspects of the proposed remedies is the wholly inadequate provisions for monitoring and enforcement. The suggested monitoring relies merely on quarterly reports prepared by Trayport's COO, a complaints procedure, and if this fails, binding arbitration '*within a reasonable period*'. A complaints procedure and subsequent arbitration would be too slow and cumbersome. The circumstances of an integrated ICE/Trayport is very different to a regulated utility network operator where access competitors can complain to a regulator and the regulator begins a dispute resolution process. These are fast-moving markets characterised by strong network effects. Dependent on the behaviour of ICE, by the time arbitration resolved any dispute, significant liquidity could have shifted away from foreclosed competing venues and significant harm done to competition. While any foreclosure target can attempt to win this volume back, it is very challenging to do so.

In addition, there would need to be, at the very least, a monitoring trustee appointed to ensure that ICE complies with the remedies, and due to the amount of data to monitor, likely a team of monitoring trustees. An *ex-post* quarterly report done by Trayport on its own would not be sufficient. The absence of a monitoring trustee makes some of the other proposals in the remedies package meaningless. For example, aside from the absence of adequate FRAND terms, which would need to be monitored on an ongoing basis, promises by ICE that Trayport will make commercially reasonable efforts to respond to requests relating to development of products or promises to honour the terms of all licenses of products cannot even be considered in the absence of reasonable monitoring provisions. A quarterly report as the only monitoring of such key aspects would be equivalent, in effect, to approving the merger unconditionally.

Proposed confidentiality firewalls would be ineffectual

It is not clear and/or detailed enough what the confidentiality firewall proposal consists of or how it will work in practice. Given Trayport senior management report directly to ICE, firewalls appear unworkable.

More specifically, the proposed ISO 27001 as protection only gives a framework for how an Information Security Management System (ISIM) is built. The utility-customised implementation still has to be done and to be defined. In particular, the controls via ICE/Trayport will have to be defined and made visual to ISMS. ISO itself gives no clear guidelines and therefore provides inadequate security. At the very least, the implementation of ISO by ICE/Trayport including the defined controls would need to be monitored. Even this gives insufficient security because it does not exclude that information will flow from Trayport to ICE. More generally, the confidentiality firewall protections offered by ICE where information is shared on a need-to-know basis, as well as a code of conduct, is meaningless without adequate monitoring. Monitoring of information flows, given the amount of sensitive information that can pass from Trayport to ICE on a day-to-day basis and the amount of information that would be expected to pass from Trayport senior management reporting to ICE, would have to be extensive

Corporate governance arrangements are permissive and leave significant residual risks

Trayport's senior management will report to ICE's data services business which themselves will report to ICE's senior management and executive board. We assume an investment of more than half a billion pounds will be discussed at an executive level within ICE. The fact that Trayport management would report to ICE's data division, rather than its Exchange C nd clearing house businesses is meaningless and inadequate. Such provisions can be easily circumvented. Even if the data services business division is not directly involved in Exchange C nd clearing, it is an integral part of ICE and it allows ICE to influence the key decision makers at Trayport. The exact role of the data division is unclear, particularly when an integral part of the actual data this division is responsible for comes from the Exchange C nd clearing businesses. Trayport senior managers will be incentivised to align Trayport operations with their boss and it will be ICE that will ultimately be judging and rewarding performance of Trayport employees.

Post-merger, the decisions made by Trayport will no longer be solely commercial decisions made in the interests of Trayport but instead will be the combined interests of ICE and Trayport, particularly where decisions that may have a negative impact on Trayport provide benefit overall to a combined ICE/Trayport group.

As only the majority of Board Members are supposed to be independent, ICE will be present at the board and will therefore obtain all Board-level information and be able to influence Trayport. Even if it does not have a formal majority on the Board, ICE's influence will be significant as the suggested minority of ICE Directors will represent the 100% owner of Trayport, which also appoints the other Directors. Much of how this will work in practice is unclear from ICE's proposals and raises a range of circumventions risks. For example, how will quorum at the Board be determined? How will voting be determined if ICE represents a majority of Board attendees, or if the Board will even decide issues by majority vote?

ICE proposes that shareholder rights will be limited to appropriate protections such as those minority shareholders are given. It is unclear how restrictions to minority shareholder rights will work at an AGM or EGM, particularly where ICE is the only shareholder, or how this prevents ICE using its (restricted) shareholder rights from exercising influence over Trayport. For example, will ICE specifically restrict its voting rights attached to its shares to less than 25% with the remainder to independent Directors? Specifically, what provisions will be subject to shareholder approval? Even if ICE did limit its voting rights ICE may still have the ability to materially influence the strategy and policy of Trayport. Minority shareholder rights can be extensive (including veto rights) and allow ICE to influence, directly or indirectly, a whole range of matters that may be put to a shareholder vote or decided by the Board. ICE will still presumably be able to exercise its (minority) shareholder voting rights as the sole shareholder over Trayport or no decision will be taken and the decision is taken by the Board. These provisions are very unclear and difficult for EXCHANGE C to provide reasoned feedback on as a result. The absence of a CEO (Trayport's CEO was fired a few days after the merger) to shape an independent strategy for Trayport is also a deep concern.

ICE's Response to the Provisional Findings

ICE's response to the Provisional Findings does not address the competition concerns identified by the CMA. EXCHANGE C believes that the merger will give rise to significant competitive harm. Our reasoning for this, which we also believe credibly rebuts many of the points ICE raises in its response, is outlined in in our previous submissions and we do not repeat these here. Nevertheless, we wanted to make a number of brief high-level points where ICE has most starkly misrepresented some of the drivers of competition, how the industry works and how foreclosure would likely occur.

ICE focuses significantly on the importance of liquidity and open interest for competition between trading venues and clearing houses, noting that these factors are unrelated to Trayport functionality. This ignores the critical role Trayport plays as a gateway and price aggregator for traders *to access the liquidity and*

open interest of competing trading venues and clearing houses. The more liquidity a venue has the more competitive it will be but it needs to be visible on the Trayport screen without delay or disruption, otherwise traders cannot access the liquidity.

To suggest that traders will be '*prevented from completing their preferred trades*' such that they will be dissatisfied with the Trayport service and switch away misrepresents how trading takes place. Traders do not have a prior preference for a trading venue but instead select the venue that offers the best prices. Trading venues are not selling cars and traders are not choosing between highly differentiated products with distinct preferences for colour, brand, interior, engine and size. If the best prices are not made available, the trader chooses the best price it can observe at the top of the stack. The fact that there may have been a better price that was not made available or delayed is not known by the trader (the second best appears the first best to the trader). The trader would naturally put this down to competing trading venues not being price competitive.

ICE argues that the foreclosure strategies are not hard to detect and as a result the losses from a foreclosure strategy are underestimated as following detection any foreclosure would risk undermining the Trayport platform. Foreclosure is not dependent on the strategies or actions being hard to detect. ICE ignores the CMA's other key point: that foreclosure would take the form of incremental changes that would not fundamentally undermine the Trayport platform. Foreclosure can be targeted at specific venues to win liquidity in specific markets – such a strategy would not undermine Trayport but can have significant effects on competing trading venues.

Consequently, ICE conflate total and partial foreclosure. A trading venue can continue to be listed on Trayport but can be listed in a way that makes it less competitive – for example, delays in displaying the pricing of certain products of certain venues. It is these types of strategies that weaken a competitor at the margin but can have a very damaging impact on competing venues but do not damage Trayport's core service proposition as described by ICE.

Further, the assertion by ICE that the foreclosure strategies (partial or total) if implemented would essentially kill the interest in Trayport Trading Gateway and lead to the risk of huge losses is false. Indeed, a useful illustrative example is Trayport having done something similar in the past by refusing to list Griffin or certain ICE products. Despite this, traders continued to use Trayport products as it already gave them access to numerous other venues. If ICE was to foreclose certain venues, traders thus would not stop using Trayport especially as they have no alternatives (due to the lack of open API allowing other ISVs).

Where foreclosure restricts traders access to liquidity of competing trading venues, the only retaliation those venues have is through fees. While fees can be used to make a venue more attractive generally these are secondary to the gains that can be made by trading a more attractive spread. The ability of competing trading venues to retaliate is therefore limited where traders' access to that venue's liquidity is impeded.

Finally, ICE has [✂].

[✂]