Anticipated acquisition by London Stock Exchange Group plc of Quantile Group Limited

Decision to refer

ME/6973/21

The CMA's decision to refer under section 33 of the Enterprise Act 2002 given on 17 May 2022. Full text of the decision published on 26 May 2022.

Please note that [✂] indicates figures or text which have been deleted or replaced in ranges at the request of the parties for reasons of commercial confidentiality.

Introduction

1. London Stock Exchange Group plc (**LSEG)** has agreed to acquire Quantile Group Limited (**Quantile)** (the **Merger**). LSEG and Quantile are together referred to as the **Parties.**

2. On 3 May 2022, the Competition and Markets Authority (**CMA**) decided under section 33(1) of the Enterprise Act 2002 (the **Act**) that it is or may be the case that the Merger consists of arrangements that are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation, and that this may be expected to result in a substantial lessening of competition (**SLC**) within a market or markets in the United Kingdom (the **SLC Decision**). Terms defined in the SLC decision have the same meaning in this decision unless otherwise specified.

3. On the date of the SLC Decision, the CMA gave notice pursuant to section 34ZA(1)(b) of the Act to the Parties of the SLC Decision. However, in order to allow the Parties the opportunity to offer undertakings in lieu of a reference to the CMA for the purposes of section 73(2) of the Act (**UILs**), the CMA did not refer the Merger for a phase 2 investigation pursuant to section 33(3)(b) on the date of the SLC Decision.

4. Pursuant to section 73A(1) of the Act, if a party wishes to offer undertakings for the purposes of section 73(2) of the Act, it must do so within the five working day period specified in section 73A(1)(a) of the Act. The SLC

Decision stated that the CMA would refer the Merger for a phase 2 investigation pursuant to section 33(1), and in accordance with section 34ZA(2) of the Act, if no undertakings for the purposes of section 73(2) of the Act were offered to the CMA by the end of this period (ie by 10 May 2022); if the Parties indicated before this deadline that they did not wish to offer such undertakings; or if the undertakings offered were not accepted.

The Proposed Undertakings

5. The SLC Decision found that the Merger gives rise to a realistic prospect of an SLC in relation to vertical effects in multilateral compression[1] for over-the-counter interest rate derivatives (**OTC IRDs**) in the United Kingdom. Multilateral compression providers for OTC IRDs such as Quantile rely on cooperation by LSEG's clearing house, LCH, to implement their multilateral compression proposals for trades cleared at LCH.[2] A multilateral compression provider that wants to offer compression of OTC IRDs cleared at LCH must be approved by LCH as an Approved Compression Service Provider (**ACSP**). Based on the available evidence, the CMA found that post-Merger LSEG would have the ability and incentive to engage in foreclosure practices targeting Quantile's rivals in the provision of multilateral compression for OTC IRDs.

6. Under section 73 of the Act, the CMA may, instead of making a reference, and for the purpose of remedying, mitigating or preventing the SLC concerned or any adverse effect which has or may have resulted from it or may be expected to result from it, accept from such of the parties concerned as it considers appropriate undertakings to take such action as it considers appropriate.

7. To address this SLC, on 10 May 2022, LSEG offered to the CMA the following behavioural undertakings for a duration of ten years (the **Proposed Undertakings**)[3], under which:

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[1] Multilateral compression is a risk-reduction technique by which a group of market participants contract with a multilateral compression provider to identify and replace multiple offsetting derivative contracts with fewer deals of the same net risk to reduce the notional value of their portfolio. By reducing the notional value of the portfolio, a customer reduces the capital that needs to be held, lowering the cost of engaging in those trades.
[2] During a run: (1) first, the ACSP informs the CCP which participants will join a particular multilateral compression run and the CCP sends the eligible trades of such participants to the ACSP; (2) the CCP also provides the present value and cashflow files for the eligible trades for the multilateral compression run and reviews the proposal to ensure that the trades are eligible; and (3) finally, the CCP determines and calls any required margin that may result from the proposal and implements the multilateral compression run.
[3] The CMA notes that the Proposed Undertakings, as submitted, would apply only to the extent that LCH is authorised or recognised to clear OTC IRDs under EMIR (Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives central counterparties and trade repositories.).

(a) LSEG would commit to approve potential or existing ACSPs based on a defined set of criteria[4] and on a non-discriminatory basis (unless objective technical requirements justify it). LSEG would be able to amend these criteria only with the approval of the monitoring trustee (the **MT**). LSEG would need to accede to or refuse a formal request for access by a potential ACSP within three months of such a request;

(b) LSEG would not engage in commercial strategies in relation to OTC IRDs cleared at LCH that apply discriminatory conditions to compression proposals from ACSPs compared to compression proposals from Quantile.[5] In particular, LSEG commits that:

(i) The ACSP fees[6] are set in a transparent manner and are non-discriminatory between ACSPs. The ACSP fees will increase [✂] for the duration of the Proposed Undertakings and changing the structure of the fees would require MT approval;

(ii) There will be non-discriminatory treatment in respect of technical specifications and operational standards that must be met by ACSPs to maintain connectivity to LCH SwapClear;

(iii) LCH processes multilateral compression files for ACSPs in the order in which these are received;

(iv) LCH confirms proposed multilateral compression cycles and publishes approved multilateral compression cycle schedules on a non-discriminatory basis between ACSPs;

(v) LCH provides ACSPs with non-discriminatory access to the trade data and the data on any changes to LCH functionality, technical specifications, operational standards, and processes in relation to the provision of clearing services for OTC IRDs necessary to offer multilateral compression.

The CMA notes that LSEG subsequently indicated that it would be willing to remove this caveat from the Proposed Undertakings, or to also include a reference to the UK equivalent legislation (UK EMIR). For all the reasons set out in this decision, the CMA does not consider it necessary to conclude whether the inclusion or removal of this language would affect its overall assessment as to the acceptability of the Proposed Undertaking, but notes that future regulatory divergence between EU EMIR and UK EMIR may create considerable additional specification risk.

[4] One of the criteria is that the potential ACSP must meet the requirements to provide multilateral compression in accordance with LCH Rulebook.

[5] LSEG would provide the MT with a compliance report (1) quarterly for the first year, (2) semi-annually for the second and third year, and (3) annually for the remainder of the period of the Proposed Undertakings.

[6] LCH charges ACSPs fees for processing their multilateral compression proposals.

(c) the MT will play a central role in resolving disputes between LSEG and potential complainants and, for the purposes of assessing whether LSEG has applied discriminatory conditions to multilateral compression proposals between Quantile and competing multilateral compression providers, would not be limited to only the criteria in paragraph 7(b)(i)-(v) above.[7]

Assessment of the Proposed Undertakings

8. In the SLC Decision, the CMA found that it is or may be the case that the Merger may be expected to result in an SLC as a result of vertical effects in multilateral compression for OTC IRDs in the United Kingdom. As set out in paragraph 5, the CMA found that, given LCH's market power in the provision of OTC IRDs clearing and the vertical relationship between multilateral compression and clearing, LCH could engage in total or partial foreclosure mechanisms targeting Quantile's rivals in multilateral compression for OTC IRDs in the United Kingdom.

9. When considering whether to accept undertakings in lieu of a reference (**UILs**) in phase 1 of its investigation, the CMA must have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the SLC and any resulting adverse effects (section 73(3) of the Act).[8]

10. Accordingly, in order to accept UILs, the CMA must be confident that all of the potential competition concerns that have been identified in its investigation would be resolved by means of the UILs without the need for further investigation. UILs are therefore appropriate only where the remedies proposed to address any competition concerns raised by the merger are clear-cut and capable of ready implementation.[9] Further:

    (a) in relation to the substantive competition assessment, the clear-cut requirement means that 'there must not be material doubts about the overall effectiveness of the remedy'; and

    (b) in practical terms, the requirement for remedies to be capable of ready implementation means that 'UILs of such complexity that their

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[7] The MT will directly deal with any allegations of non-compliance of the Proposed Undertakings relating to confirmation of multilateral compression cycles, publication of multilateral compression schedules and changes to the schedule on non-discriminatory terms. Any other allegation raised by a complainant will be first escalated to the Group Head of Post Trade and will need to be settled within 25 days. Absent agreement, the MT will decide the matter.
[8] Mergers remedies (CMA87), December 2018 (Remedies Guidance), paragraph 3.30.
[9] Remedies Guidance, paragraph 3.27.

implementation is not feasible within the constraints of the Phase 1 timetable are unlikely to be accepted'.[10]

11. At phase 1, the CMA is generally unlikely to consider that a behavioural undertaking will be sufficiently clear-cut to address the identified competition concerns as it will not address the SLC at source (unlike a structural remedy), may give rise to a number of risks which can reduce its effectiveness or create competition concerns elsewhere, and can be difficult to monitor and enforce.[11] Nevertheless, despite its preference for structural remedies, the CMA will not inevitably refuse behavioural remedy offers, in particular where a structural remedy would be clearly impractical or is otherwise unavailable.[12]

12. The CMA has material doubts that the Proposed Undertaking would effectively remedy the competition concerns identified in the SLC Decision. The CMA's starting point in deciding whether to accept UILs offered is to seek an outcome that restores competition to the level that would have prevailed absent the merger, thereby comprehensively remedying the SLC (rather than accepting a remedy that simply mitigates the competition concerns).[13]

13. As set out below, the CMA believes that there is a material gap between the pre-Merger situation and what the Proposed Undertakings attempt to achieve. The CMA has material concerns in a number of areas of the Proposed Undertakings, each of which would significantly undermine their effectiveness. These include:

    (a) Based on the available evidence, it is uncertain whether the duration of the Proposed Undertakings suffices to address the SLC. In line with its Guidance, the CMA will generally only use behavioural remedies as the primary source of remedial action in a limited set of circumstances, such as those where the SLC is expected to have a short duration.[14] In the present case, there is no evidence that the SLC would be time limited. Furthermore, for a remedy to be considered clear-cut, the CMA considers that it is not appropriate to rely on future events or future actions taken by third parties (eg entry or expansion or regulatory changes) for which the CMA cannot be sufficiently certain as to their occurrence, timing, or sufficiency.[15] The CMA, therefore, believes that the Proposed Undertakings are not clear-cut and effective given their limited duration.

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[10] Remedies Guidance, paragraph 3.28.
[11] Remedies Guidance, paragraphs 3.5(a) and (c) and 3.32.
[12] Remedies Guidance, paragraph 3.32.
[13] Remedies Guidance, paragraphs 3.27 to 3.28 and 3.30 to 3.31.
[14] Remedies Guidance, paragraph 7.2.
[15] ME/6905/20, Tronox Holdings/TiZir Titanium & Iron (2021), paragraph 11 (a).

(b) Under the Proposed Undertakings, LSEG is able to treat differently providers of multilateral compression services provided this is justified by 'objective technical requirements'. The CMA considers that 'technical requirements' is an unclear term which renders the form of conduct required to address the SLC uncertain.[16] Second, as set out above, based on the Proposed Undertakings, LCH will approve an ACSP if it meets the requirement to provide multilateral compression in accordance with the LCH Rulebook. The Proposed Undertakings do not, however, effectively cover amendments to the LCH Rulebook outside of reporting changes to the MT.[17] The CMA, therefore, believes that the Proposed Undertakings would not prevent LCH from changing the LCH Rulebook to make ACSP approval more arduous. The CMA further notes that while the supervision of the MT might mitigate this concern, it would not fully address it. For these reasons, the CMA believes that the Proposed Undertakings are not sufficiently precise to provide an effective basis for specification, monitoring, and compliance.

(c) The Proposed Undertakings include a general commitment by LSEG not to engage in commercial strategies in relation to OTC IRDs clearing that apply discriminatory conditions to multilateral compression proposals from ACSPs compared to multilateral compression proposals from Quantile. According to the Parties, this commitment is drafted broadly to prevent foreclosure mechanisms not covered by the Proposed Undertakings, including foreclosure mechanisms that the CMA did not explicitly identify in its SLC decision. The CMA does not consider that this commitment would be effective in preventing foreclosure, because:

(i) The definition of 'discrimination' is unclear and, therefore, market participants would not be able to detect LSEG's non-compliance with the Proposed Undertakings. While the CMA accepts that the concept of discrimination is used in a number of regulatory contexts, as well as in competition law[18], the CMA considers that the precise definition

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[16] Specification risks arise if the form of conduct required to address the SLC or its adverse effects cannot be specified with sufficient clarity to provide an effective basis for monitoring and compliance (Remedies Guidance, paragraph 7.4 (a)).
[17] See footnote 5. The CMA does not agree with LSEG's submission that the MT would be able to consider a change to the LCH Rulebook to determine whether it is discriminatory and in breach of the commitments, because LSEG's obligations regarding the LCH Rulebook are limited to: (1) complying with the rules set out in the LCH Rulebook (but not that its rules are themselves non-discriminatory), and (2) reporting on LCH Rulebook changes to the MT at increasingly lengthier intervals.
[18] The Parties submitted that the concept of discrimination is understood as a matter of competition law as it is mentioned both by chapter 2 CA98 and paragraph 7.21 of the Remedies Guidance which relate to the provision of products on fair, reasonable and non-discriminatory terms. The Parties further submitted that non-discrimination is also a concept that is used extensively throughout financial regulation which applies to both LSEG and the LCH Group and as such is well understood by both the Parties and the market participants including Quantile's rivals.

of discrimination is heavily dependent on the regulatory regime at issue and, even in the field of competition law, is often contested or difficult to precisely define.[19]

(ii) The general non-discrimination commitment would apply only to conduct that affects 'Compression Proposals', defined under the Proposed Undertakings as the 'final statement as to the proposed set of terminating SwapClear contracts and the proposed set of resulting contracts'. The CMA considers that there are various mechanisms of foreclosure (including several mechanisms explicitly mentioned by LSEG in the Proposed Undertakings such as those that relate to access to trade data and other sensitive information necessitating firewalls) that would not be considered discrimination as to the final 'Compression Proposals', as they would not themselves affect the final statement of terminating contracts and the proposed set of resulting contracts.

(d) The Proposed Undertakings also entail significant monitoring and enforcement risks, which would result in material doubts over the implementation of the Proposed Undertakings. In particular:

(i) For all forms of partial foreclosure outside of the limited explicit commitments set out in the Proposed Undertakings[20], the ability to require LSEG not to engage in discriminatory conduct would require the MT to determine that LSEG had discriminated against a multilateral compression provider and, as currently drafted, only in the narrow case of 'Compression Proposals' (see paragraph 13 (c)(ii)).

(ii) To the extent the Proposed Undertakings could be interpreted as preventing LSEG from engaging in other foreclosure mechanisms, this would require significant case-by-case assessment by the MT in a quasi-regulatory process, which would only take place, in most instances[21], after a multilateral compression provider had exhausted attempts at resolving issues with LCH, and would require the MT to

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[19] The CMA notes that the concept of 'discrimination' is not clear-cut within the context of chapter 2 CA98 as submitted by the Parties, in so far as it requires an assessment of three separate sets of highly fact-specific criteria; namely whether there are 'dissimilar conditions' between 'equivalent transactions' that result in a 'competitive disadvantage'. The CMA further notes that in regulated sectors, this question often falls to a specialist competition/economic regulator empowered to give binding rulings or adjudicate and clarify (eg in guidelines) how the concept of 'discrimination' should be understood in a particular sector.
[20] The CMA notes that there are specific commitments where the MT plays a more active role in policing foreclosure that do not require a dispute to be brought to the MT, but instead require the MT's explicit approval. For instance, the Proposed Undertakings provide that any changes to the structure of LSEG's ACSP fees requires MT approval.
[21] See footnote 7.

establish all the relevant facts and carry out its own determination of whether the conduct at issue is in fact discriminatory.

(iii) The CMA considers that a MT defining and policing the extent of any discrimination LSEG engages in would impose a potentially severe monitoring and enforcement burden on the MT, as well as the CMA, who would expect to be involved in assessing discrimination for significant or novel disputes, which would itself necessitate a mechanism by which the CMA and MT could identify which disputes warranted the CMA's involvement. The risk that this mechanism would fail to operate effectively to address discrimination is material, giving rise to serious doubts as to the efficacy of the remedy.

14. Therefore, the CMA considers that the Proposed Undertakings raise serious risks relating to specification, circumvention, monitoring and enforcement and that as a result of each of the issues set out above, the Proposed Undertakings do not consist of a clear-cut solution to the competition concerns identified in the SLC Decision.

15. More fundamentally, even if LSEG were to address each of the above points to the CMA's satisfaction, the CMA would expect to continue to have serious concerns as to whether the Proposed Undertakings would represent a clear-cut remedy at the phase 1 standard. This is because the CMA considers the very breadth and generality of the commitments, which the CMA understands LSEG has proposed in an attempt to cover all potential foreclosure mechanisms (including potential future foreclosure mechanisms), would themselves constitute unacceptable specification, circumvention, and monitoring and enforcement risks, in that they avoid specifying the precise behavioural conduct necessary to remedy the SLC, and that the Proposed Undertakings instead places a quasi-regulatory burden on the MT (and in turn on the CMA).

Decision

16. For the reasons set out above, after examination of the Proposed Undertakings, the CMA does not believe that it would achieve as comprehensive a solution as is reasonable and practicable to the SLC identified in the SLC Decision and the adverse effects resulting from that SLC.

17. Accordingly, the CMA has decided not to exercise its discretion under section 73(2) of the Act to accept undertakings in lieu of reference.

18. Therefore, pursuant to sections 33(1) and 34ZA(2) of the Act, the CMA will proceed to refer the Merger to its chair for the constitution of a group under Schedule 4 to the Enterprise and Regulatory Reform Act 2013 to conduct a phase 2 investigation.

David Stewart
Executive Director, Markets and Mergers
Competition and Markets Authority
17 May 2022