CMA
Competition & Markets Authority

COMPLETED ACQUISITION BY INTERCONTINENTAL EXCHANGE, INC. (ICE) OF TRAYPORT

ISSUES STATEMENT

31 May 2016

The reference

1. On 3 May 2016, the Competition and Markets Authority (**CMA**), in exercise of its duty under section 22(1) of the Enterprise Act 2002 (the **Act**), referred the completed acquisition by Intercontinental Exchange, Inc. (**ICE**) of Trayport, Inc. and GFI TP Ltd., including their subsidiaries (together **Trayport**) (the **Merger**), for further investigation and report by a group of CMA panel members (the **Group**).

2. In exercise of its duty under section 35(1) of the Act, the CMA must decide:

   (a) whether a relevant merger situation has been created; and

   (b) if so, whether the creation of that situation has resulted, or may be expected to result, in a substantial lessening of competition (**SLC**) within any market or markets in the UK for goods or services.

3. In answering these two questions we will apply a 'balance of probabilities' threshold to our analysis, that is, we will decide whether it is more likely than not that an SLC will result from the Merger.[1]

4. In this statement, we set out the main issues we are likely to consider in reaching our decision on the SLC question (paragraph 2(b) above), having had regard to the evidence available to us, including the evidence referred to in the CMA's phase 1 decision to refer the Merger for further investigation (the **Phase 1 Decision**).[2] This does not preclude the consideration of any other issues which may be identified during the course of our investigation.

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[1] *Merger Assessment Guidelines* (CC2/OFT1254), paragraph 2.12. The *Merger Assessment Guidelines* have been adopted by the CMA Board (see *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), Annex D).
[2] See the full text decision on the case page.

5. Throughout this document we refer to ICE and Trayport collectively as 'the **Parties**' and to the combined entity as 'the **Merged Entity**' where appropriate.

Background

6. On 11 December 2015, ICE completed its acquisition of Trayport from BGC Partners and GFI. The Merger was an acquisition of sole control of Trayport by ICE for approximately $650 million, comprising approximately 2.5 million ICE common shares as consideration. The CMA opened an own-initiative investigation into the Merger by sending an enquiry letter to ICE on 5 January 2016.[3]

7. ICE is a global operator of exchanges and clearinghouses, and as part of its activities facilitates trading of energy commodities and utilities derivatives. In Europe, its exchanges include ICE Futures Europe and ICE Endex, where trades in natural gas, power (electricity), coal and emissions and related derivatives take place. ICE Endex is a host to the UK, Dutch and Belgian natural gas spot markets. ICE Clearing Europe is the clearinghouse for the above mentioned exchanges.

8. Trayport licenses software products to participants (traders, brokers, exchanges and clearinghouses) active in the wholesale markets for European utility derivatives and commodities (in particular, natural gas, power, oil, coal and emissions). Trayport operates the primary gateway, or '**front-end'** screen, used by traders to initiate trading of energy commodity derivatives over the counter (**OTC**), that is, through brokers, and on some exchanges. Trayport also facilitates electronic and hybrid derivatives trading through the provision of a software infrastructure, or **'back-end'**, used by brokers and exchanges (brokers and exchanges are together referred to as '**trading venues'**) for the purposes of supplying execution services to traders. Trayport's other core software service provides a straight-through-processing (**STP**) solution which allows traders to submit trades conducted off-exchange via a broker for central clearing.

9. A more detailed description of the Parties and their activities can be found at paragraphs 39 to 47 of the Phase 1 Decision.

10. The Parties overlap in the supply of energy trading front-end access services (or screens) to traders (for more details see paragraphs 22, 117 and 118 of the Phase 1 Decision). Trayport also provides an important software input into the activities of brokers, exchanges and clearinghouses, which are rivals of

[3] See *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), paragraphs 6.9–6.19 & 6.59–60.

ICE in the supply of execution services (by brokers and exchanges) and clearing services (by exchanges' clearinghouses) of OTC executed trades.

Market definition

11. The purpose of market definition is to provide a framework for the analysis of the competitive effects of a merger. The relevant market contains the most significant competitive alternatives available to the customers of the merger firms and includes the most relevant constraints on the behaviour of the merger firms.[4] However, the boundaries of the market do not determine the outcome of the CMA's analysis of the competitive effects of the merger in any mechanistic way. In assessing whether a merger may give rise to an SLC, the CMA may take into account constraints outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others.[5]

12. As set out above, the Parties both supply front-end trading screens to energy traders, and Trayport supplies an important software input(s) into the activities of brokers, exchanges and clearinghouses (more details are provided in the section on 'Theories of harm to be investigated by the CMA' set out below). Therefore, the CMA will consider market definition by reference to the products where the Parties' activities overlap, and also by reference to the products supplied by Trayport to brokers, exchanges and clearinghouses, each being rivals of ICE. Specifically, we will consider the appropriate market definition for the purposes of assessing the Merger by reference to the following categories of services:

    (a) Supply of energy trading front-end access services to traders.

    (b) Supply of back-end technology to OTC brokers and exchanges, respectively.

    (c) Supply of access services to clearinghouses for OTC executed trades.

    (d) Supply of trade execution services to traders.

    (e) Supply of trade clearing services to traders.

13. For the supply of front-end access services (see paragraph 12(a) above), as part of our assessment we will consider the extent to which there is any price or service competition between Trayport's front-end screens, '**Joule/Trading Gateway**', and ICE's front-end screen, '**WebICE**', and to the extent there is

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[4] *Merger Assessment Guidelines*, paragraph 5.2.1.
[5] *Merger Assessment Guidelines*, paragraph 5.2.2.

whether as a result of a pre-Merger price increase and/or a deterioration in quality of service traders would have switched between the two. We will also consider whether any profit lost on sales to customers that switch to rivals would be sufficient to make any price rise/service quality deterioration unprofitable.[6] We will carry out this assessment separately for each Party in order to take into account the possibility that any competitive constraint pre-Merger may have been asymmetric, that is, the extent to which traders would switch from Joule/Trading Gateway to WebICE may differ from the extent to which traders would switch from WebICE to Joule/Trading Gateway.

14. For each of the category of services listed in paragraph 12 above, the CMA will also consider whether the effects of the Merger on competition may vary by '**asset class**' (eg power, gas, electricity, emissions, etc) and by '**product**' (eg spot contracts, forwards, futures, etc.).

15. For the geographic market definition, the CMA will consider whether it is national, EU or EEA-wide or broader, and whether the geographic market definition may vary by asset class and/or product type.

Assessment of the competitive effects of the Merger

Counterfactual

16. We will assess the potential effects of the Merger on competition compared with the competitive conditions in the counterfactual situation (ie the competitive situation absent the Merger). We will therefore consider what would have been most likely to have happened if the Merger had not taken place, and in particular whether:

    (a) the vendors would have retained ownership of Trayport and continued to operate it as before; or

    (b) if the vendors had been unlikely to retain ownership of Trayport:

        (i) whether at the time of the sale there would have been other likely buyers for all or part of the Trayport business; and

        (ii) whether such buyers would have been likely to lead to competition concerns.

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[6] *Merger Assessment Guidelines*, paragraph 5.2.11–5.2.13.

17. In making our assessment, we will consider possible alternative scenarios and decide upon the appropriate counterfactual situation based on the facts available to us and the extent to which events or circumstances and their consequences are foreseeable.[7]

Theories of harm to be investigated by the CMA

18. Theories of harm describe the possible ways in which an SLC may be expected to result from a merger, and provide the framework for our analysis of the competitive effects of a merger. We have set out below the theories of harm that we are currently minded to investigate. However, we may revise our theories of harm as our inquiry progresses. The identification of a theory of harm does not preclude an SLC being identified on another basis following further work by us, or the receipt of additional evidence.

19. We are currently considering one horizontal theory of harm and two vertical theories of harm.

20. The concern under a horizontal (unilateral) effects theory of harm is that the removal of one party as a competitor could allow the merged entity to increase prices, lower quality, reduce the range of their services and/or reduce innovation, all relative to the counterfactual.

21. The concern under a vertical theory of harm is that bringing together the merging parties creates or increases the ability or incentive of the merged entity to harm competition at one level of the supply chain through its behaviour at another level of the supply chain.

22. In addition to considering each theory of harm separately, we will also consider how the theories interact, and consider the effect of the merger in the round. We welcome views on all the theories of harm set out below.

Theory of harm 1: unilateral horizontal effects arising from the loss of actual competition in the supply of energy trading front-end access services

23. We will examine whether the Merger results or may be expected to result in an SLC as a result of horizontal unilateral effects in the supply of energy trading front-end access services.

24. Trayport supplies 'Joule', a front-end trading screen that connects to Trayport's Trading Gateway, which aggregates pricing and volume information from multiple trading venues and orders it according to time of

[7] *Merger Assessment Guidelines*, paragraph 4.3.2.

entry and other variables. Trayport also supplies a screen that allows traders to access a single trading venue (ie one broker or one exchange) at a time.

25. ICE supplies its own front-end screen called WebICE, which currently provides traders with access to ICE's exchanges only. ICE's exchanges can also be accessed via 'conformed' third parties (ie independent software vendors (**ISVs**) or ICE customers who have developed their own in-house software) that allow traders to view ICE's real time market data and execute trades on ICE's exchanges.

26. We will assess whether, as a result of the loss of competition between the Parties, the Merged Entity could increase the prices of its products, deteriorate the quality of its service offering and/or reduce innovation. In general, for this theory of harm to be substantiated, the following three conditions must be met:

(a) The Parties were close competitors pre-Merger in the supply of energy trading front-end access services from the perspective of traders. In particular, we will consider:

(i) the extent to which front-end screens that provide access to a single venue (similar to WebICE) and front-end screens that provide access to multiple venues (similar to Joule/Trading Gateway) are considered substitutes from the perspective of traders;

(ii) the extent to which ICE and other exchanges available via Trayport are considered substitute execution venues from the perspective of traders; and

(iii) the extent to which ICE and brokers available via Trayport are considered substitute execution venues from the perspective of traders.

(b) There are no rivals likely to be able to replace the competitive constraint that the Parties exerted on one another pre-Merger, or that one Party exerted on the other if they constrained each other asymmetrically,[8] in the supply of energy trading front-end access services.

(c) There are no rivals that are likely to enter or expand in the market for the supply of energy trading front-end access services within a reasonable timeframe and which can replace the competitive constraint lost through

[8] There could still be anti-competitive effects if pre-Merger competition between WebICE and Joule/Trading Gateway is asymmetric, that is, one party exerts a significant constraint on the other party but less so in the opposite direction.

the Merger. Further consideration of this is sent out in the section on 'Countervailing Constraints' below.

27. The CMA will consider whether its assessment would vary by asset class and/or product. The CMA will also take this approach for each of the vertical theories of harm listed below.

28. We will also consider the relevance of Trayport's closed system strategy, which is set out in more detail at paragraph 32 below.

Theory of harm 2: vertical effects arising through input foreclosure of competing trading venues (ie exchanges and brokers)

29. We will examine whether the Merger may be expected to result in an SLC as a result of vertical foreclosure, including total foreclosure where the Merged Entity may stop supplying Trayport's software to trading venues altogether, or partial foreclosure of trading venues where the Merged Entity may increase prices and/or reduce service quality. We will consider the foreclosure of exchanges and brokers separately.

30. Trayport provides software to trading venues (ie brokers and exchanges) that compete with ICE (the operator of a number of exchanges) for the execution of trades. In particular, Trayport provides the back-end technology used by trading venues to execute trades in the energy market. In the case of brokers, this software technology is the GlobalVision Broker Trading System (**BTS**); for exchanges it is the GlobalVision Exchange Trading System (**ETS**).

31. Three necessary conditions need to be met for this vertical theory of harm to hold:

    (a) **Ability** – will the Merged Entity have the ability to harm competitors? To answer this question we will consider:

        (i) the mechanisms through which the Merged Entity could harm competitors, eg a price increase, a worsening of the quality of services offered by the Merged Entity to trading venues (eg degrading the support to Trayport's software and/or de-prioritising product development), or by refusing to supply Trayport's software, etc;

        (ii) the alternatives available to the services offered through Trayport's software to trading venues and the costs of switching;

        (iii) whether trading venues using Trayport's software could switch to these alternatives; and

(iv) whether there are any barriers to entry and expansion in the provision of software to trading venues. This will include an assessment of the degree of functional integration between back-end and front-end.

(b) **Incentives** – will the Merged Entity have the incentive to harm competitors? To answer this question we will consider:

(i) the extent to which ICE could divert substantial trading volumes to its own exchanges by implementing a foreclosure strategy;

(ii) the Parties' revenue streams, their key drivers and relative size in order to understand the profits that the Merged Entity would gain and lose from foreclosing trading venues; and

(iii) whether ICE is a close competitor of the trading venues that use Trayport's software. This is relevant to understanding whether traders would divert their trades to ICE if its rivals' offerings were to worsen/degrade and, consequently, whether ICE could gain additional revenue from harming some of the trading venues that use Trayport.

(c) **Effect** – will harm to competitors result in harm to competition? To answer this question we will consider:

(i) whether the Merged Entity will have the ability to foreclose a sufficient number of trading venues in order for such a strategy to have a substantial effect on competition;

(ii) whether any of ICE's rivals have their own proprietary software (ie operate a vertically integrated model) and would not be harmed by any foreclosure strategy; and

(iii) whether there are any efficiencies arising from the Merger that may enhance rivalry.

32. As part of our considerations, we will also consider what commercially sensitive data ICE will have access to as a result of its ownership of Trayport and the extent to which this information could be used by the Merged Entity to its competitive advantage and/or as part of any foreclosure strategy. We will review the extent to which contracts entered into by Trayport with trading venues may militate against the inappropriate use of sensitive trading data, and any other possible mechanisms that the Merged Entity could use to harm its rivals. However, as its usual practice, the CMA will attach caution to its

assessment of any contractual protections noting that the contract durations may not be long-term and any terms may vary.

33. We will also consider the relevance of Trayport's closed system strategy (sometimes referred to as a closed access programming interface (**Closed API**)), which means that the brokers and exchanges that use Trayport's back-end (ie BTS and ETS) are accessible to traders only through Trayport's front-ends. This means that if traders want to see and execute trades via any of the trading venues that use Trayport's back-end they have to use one of the front-end solutions offered by Trayport (ie Trading Gateway/Joule or the direct screens that give access to traders only to one trading venue). This situation existed pre-Merger and, therefore, we will consider whether there are any merger specific effects which may arise from this Closed API strategy, eg will it make it easier for the Merged Entity to implement the mechanisms through which the Merged Entity could foreclose competitors.

Theory of harm 3: vertical effects arising through input foreclosure of competing clearinghouses

34. We will examine whether the Merger may be expected to result in an SLC as a result of vertical foreclosure of clearinghouses.

35. ICE owns and operates a clearinghouse through which all trades executed on ICE exchanges are cleared. Trades executed OTC can also be registered and subsequently cleared through ICE clearinghouse.

36. Trayport provides an STP solution to clearinghouses that compete with ICE. This automatically connects clearinghouses to brokers so that trades executed OTC can be cleared automatically without manual input, subject to the trader's choice of clearing house.

37. For this theory of harm to hold, the three conditions set out in paragraph 31 will need to be met in the context of the provision of clearing services for OTC executed trades. We will take forward the same set of considerations as set out in that paragraph.

38. For both vertical theories of harm, we will also consider any broader strategic considerations, such as reputational effects, and the link between front-end screens, back-end software (and the execution of trades) and the provision of clearing services, which may affect the Merged Entity's behaviour.

Countervailing factors

39. We will consider whether there are countervailing factors which are likely to prevent or mitigate any SLC that we may find.

Entry and expansion

40. We intend to consider whether entry or expansion by effective competitors could be expected to be timely, likely and sufficient to prevent any SLC. To do this, we will in particular:

    (a) look at the history of actual entry, expansion and exit by the Parties and by their competitors (including any repositioning of their offering) and review any future plans;

    (b) consider the costs and time necessary for competitors to develop and launch new front-end technology and/or back-end software technology; and

    (c) examine other factors that might inhibit entry or the expansion of existing competitors, such as liquidity concentration and the degree of functional integration between back-end and front-end, including consideration of Trayport's 'closed API' strategy discussed above.

Efficiencies

41. We will also examine any evidence available to us in relation to efficiencies arising from the Merger. In particular, we will examine whether there are Merger-specific rivalry enhancing efficiencies that can be expected to mean that the Merger would not result in an SLC.

Buyer power

42. We will assess whether any customers of Trayport and ICE have countervailing buyer power, and whether the buyer power of these customers would be sufficient to protect customers from any effects of an SLC. We will also consider the likely impact of the Merger on any pre-existing countervailing buyer power.

Possible remedies and relevant customer benefits

43. Should we provisionally conclude that the Merger may be expected to result in an SLC in one or more markets, we will consider whether, and if so what, remedies might be appropriate, and will issue a further statement.

44. In any consideration of possible remedies, we may in particular have regard to their effect on any relevant customer benefits that might be expected to arise as a result of the Merger and, if so, what these benefits are likely to be and which customers would benefit.

Responses to the issues statement

45. Any party wishing to respond to this issues statement should do so in writing, by no later than **5pm on 14 June 2016**. Please email ice.trayport@cma.gsi.gov.uk or write to:

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