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Success and failure in stock exchange consolidations: Implications for markets and their regulation

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SUCCESS AND FAILURE IN STOCK EXCHANGE CONSOLIDATIONS: IMPLICATIONS FOR MARKETS AND THEIR REGULATION

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The usual disclaimers apply.

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INTRODUCTION^{*}

The catalyst for the preparation of this working paper was the epochal merger in 2007 of the New York Stock Exchange with Paris-based Euronext, itself a consolidation of several European exchanges. Exchange mergers were not a new phenomenon; domestic and regional exchanges had been consolidating for decades. However, NYSE Euronext was the big deal, creating, for a time at least, the largest exchange in the world and linking, for the first time, the United States and Europe. The NYSE Euronext merger appeared like a bolt out of the blue, the exchanges coming together with astonishing rapidity, bedeviling and outpacing pundits and regulators alike. This was the game changer; the truly global exchange could not be far behind. Partly as a defensive strategy, other exchanges scrambled to forge alliances and a sometimes frenzied courting game ensued.

The original intent behind this project was to investigate why some consolidations succeeded whereas others failed and the market and regulatory implications of success or failure. As the research proceeded however, it became apparent that the forces driving exchange consolidations were foundering. Demutualisation had provided the merger currency and theoretically at least facilitated the process. However, demutualisation also created those pesky shareholders that could stymie the best laid merger plans. Rhetoric as to the ‘mergers of equals’, as in the Toronto-London or Sydney-Singapore merger talks, often rang hollow. After chasing the ‘big fish’ (the London Stock Exchange), NASDAQ changed course and contented itself with hovering up little fish such as OMX and Dubai. Some exchanges (London, Frankfurt), at least at times, glorified their position of splendid isolation and old rivalries died hard. Asian exchanges for the most part, Singapore being the exception, appeared indifferent to the merger frenzy. They were not much interested in derivatives trading, one of the factors behind some merger talks.

Politics inevitably played a role. Strong self-regulatory traditions could assist exchanges in sidestepping many formal regulatory impediments, but there was always the possibility of a joker in the pack in the form of ‘national interest’ concerns. Stock exchanges can be powerful national symbols, and governments reluctant to relinquish them. The ‘public utility’ function of the exchange lingered, raising concerns as to foreign ownership and control. The

^{*} The author would like to thank Marco Garofalo (Faculty of Law, McGill University), and Brendan Donohue and Sahil Sondhi (formerly, Melbourne Law School), for their able assistance in the preparation of this introduction. Parts of this introduction appear in ‘Stock Exchanges: An Endangered Species’ in Cally Jordan, *International Capital Markets: Law and Institutions* (Oxford University Press, 2014) ch 10.

Australian Treasury nixed the Singapore-Sydney merger; a consortium of banks and institutional investors, calling themselves ‘Maple’, draped themselves in the Canadian flag to defeat the London-Toronto deal.

The exchanges were chasing growth through diversification across product and territorial borders, in the hopes that scale would increase revenue and reduce costs. But markets were changing rapidly. The main competitors to any exchange were no longer other exchanges; rather, alternative trading platforms, more or less fancy free from a regulatory perspective, were poaching trading volume from the traditional exchanges. But the technology creating alternative trading platforms also provided alternative strategies to formal mergers and without the political headaches associated with them. The business model of the exchange was changing with the markets. Formal mergers, with their very public displays of dominance, gave way to discreet strategic alliances and compatible trading platforms.

And, of course, some mergers were simply impossible, at least for the time being. Shanghai-Hong Kong and Shenzhen-Hong Kong have no choice but to settle for something less than a formal merger. There is no prospect of a China Stock Exchange in the near future. The organisational form and regulatory context of these exchanges remain too different.

The goal of this working paper is modest. It attempts to document the recent phenomenon of stock exchange mergers, successful, but for the most part, unsuccessful. The paper provides a short summary of the origins and history of several exchanges engaged in the mating games. In order to assist in keeping the record straight as to who was making passes at whom and when and where, the paper provides a detailed timeline of the major merger activity over the last decade. The major portion of the paper is devoted to case studies of several mergers or merger alternatives, concluded or proposed. The anchor story, of course, is the rise and demise of NYSE Euronext. In terms of significance, London and its passage from splendid isolation to both hunter and hunted, comes next. The NASDAQ story is a brief, and likely disappointing, one, at least to NASDAQ. The outcomes for Toronto and Sydney were similar, but the dynamics of their stories very different. In these times, no story is complete with a consideration of China. There are other stories, of course, and other lessons to be learned.

I BACKGROUND

Among capital market institutions, exchanges are the most visible and vocal.¹ Despite the waves of demutualisation² and consolidation, exchanges remain idiosyncratic institutions. Even where similar structural reorganisations have occurred, the underlying factors prompting such moves, and potentially the on-going operations of the exchanges, are often quite different. Some exchanges, such as Luxembourg and Switzerland, proudly assert their independence, bucking the trend towards either consolidation or demutualisation. Nor is there convergence to an optimal model going on here. As IOSCO concluded in its 2006 study on the evolution of exchanges, ‘steps taken have tended to be customized and pragmatic, based on an assessment of the particular circumstances in a jurisdiction’.³

Nor do market forces alone determine the nature of exchanges and their regulation. As capital markets grew in importance, the role of exchanges extended beyond that of a trading venue. The modern exchange also serves political masters, acting as a national symbol in some cases, and thus eliciting regulatory responses not based on market considerations alone. More importantly, exchanges are imbued, implicitly or explicitly, with a ‘public interest’ due to their impact on the related issues of economic growth, systemic financial stability and investor protection.

But herein lies a conundrum. The traditional exchange, even the most up to date, is a vulnerable species. Anyone with a computer can create an exchange; what is more, it can have global reach. Trading is migrating away from formal exchanges to alternative trading platforms.⁴ Despite consolidation at the exchange level, multiple electronic trading venues are splintering the market. High frequency trading is driving institutional investors, who tend to hold large positions and relatively long term views, off the exchanges and into the ‘dark pools’.⁵ As the exchange has been the foundation stone of market institutions, the regulatory consequences of this shift are profound and still unappreciated. Even regulatory changes as

¹ See Cally Jordan and Pamela Hughes, ‘Which Way for Market Institutions? The Fundamental Question of Self-Regulation’ (2007) 4 *Berkeley Business Law Journal* 205.

² See definition of ‘demutualisation’, below n 19.

³ Technical Committee, International Organization of Securities Commissions (IOSCO), ‘Regulatory Issues Arising from Exchange Evolution’ (Consultation Report, IOSCO, March 2006) 28 <<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD212.pdf>>.

⁴ In Europe, this trend is pronounced. This may be a reaction to the historically high trading costs associated with the multiplicity of exchanges in Europe and the structural impediments to cross-border trading.

⁵ In 2010, NASDAQ OMX, itself a transatlantic consolidated exchange, created a new platform, PBX, in an attempt to regain trading volume by institutional investors placing large orders in the dark pools.

recent as 2008, designed to adapt regulation to the electronic age, are now out-dated because of their assumptions about exchange trading.⁶

In addition to undermining the price discovery mechanism of exchanges,⁷ the alternative trading platforms and other electronic markets may have little concern for the public interest. The notion of public interest justifies the application of regulation to exchanges. Yet, what is considered in the public interest, and how best to promote it, varies considerably from place to place.

Notions of public interest may also be highly culturally or politically specific and notoriously difficult to define with precision. The operation of public interest is more circumscribed in the United States than, say, in Singapore. In a fashion similar to German and Canadian law,⁸ Hong Kong and Singapore both explicitly posited a public interest function in the legislation authorising the demutualisation of their exchanges.⁹

Among exchanges, there is also a definite, and dynamic, hierarchy. A few major exchanges dominate (the former NYSE Euronext, LSE, NASDAQ OMX, Deutsche Börse). In just a handful of years though, newcomers have joined the upper echelons: the HKEx in Hong Kong, for example, and the CME Group, the Chicago-based commodities and derivatives exchange.

These exchanges share in the headlines, but differ greatly among themselves. The LSE is the most internationalised equities exchange. The NYSE component of NYSE Euronext, especially after the takeover by Atlanta based upstart, Intercontinental Exchange (ICE), is the

⁶ *Securities Exchange Act of 1934*, 15 USC §12g3-2(b) (1934), applicable to non-US issuers, was updated 2008 to substitute public information made available on company websites for paper filings with the SEC, but made conditional on listing on an overseas exchange. With European trading shifting markedly off-exchange, many issuers may now fall outside Rule 12g3-2(b).

⁷ See also: the Efficient Market Hypothesis. For a good survey article, see Burton G Malkiel and Eugene F Fama, 'Efficient Capital Markets: A Review of Theory and Empirical Work' (1970) 25 *Journal of Finance* 383.

⁸ Ontario Securities Commission, *Securities Law & Instruments*, NI 21-101 — *Marketplace Operation* <<https://www.osc.gov.on.ca/en/13537.htm>>, states that the rules and policies of an exchange must not be contrary to the 'public interest' and must be designed to prevent fraudulent practices and promote 'just and equitable' principles of trade. Additionally, NI 21-101 introduces rules that prohibit an exchange from using its position to limit competition from other exchanges or ATSS, or unreasonably deny access to its services.

⁹ Andreas M Fleckner, 'Stock Exchanges at the Crossroads' (2006) 74 *Fordham Law Review* 2541; See also John W Carson, 'Conflicts of Interest in Self-Regulation: Can Demutualized Exchanges Successfully Manage Them?' (Policy Research Working Paper No 3183, World Bank, December 2003) <<http://econpapers.repec.org/paper/wbkwbrwps/3183.htm>>; Technical Committee, International Organization of Securities Commissions (IOSCO), 'Responses to the IOSCO Consultation Report Entitled Regulatory Issues Arising from Exchange Evolution' (Publication, June 2006) 20-25 <<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD221.pdf>> (Deutsche Börse notes the requirements of German law with respect to the public interest function of exchanges); Technical Committee, International Organization of Securities Commissions (IOSCO), 'Regulatory Issues Arising from Exchange Evolution', above n 3, 33 (the French Association of Investment Firms discusses the public interest implications of exchanges and they note it is a 'situation that demands appropriate governance arrangements and close regulatory scrutiny').

largest in the United States which in turn is the world's largest domestic market. Deutsche Börse vies with London as the largest in Europe. NASDAQ OMX is the major alternative to the NYSE in the United States (at least for equities), favoured by technology firms, and engaged in numerous international dalliances. The Tokyo Stock Exchange, recently dethroned by HKEx, used to be the largest in Asia, yet remained stubbornly a domestic market. HKEx is the gateway to China. The rise of the CME reflects the increasing importance of non-equity based financial instruments. Euronext, after several marriages of convenience, surged (at least temporarily) to prominence due to its troubled merger with the NYSE. These exchanges can afford tailor-made regulatory regimes to suit the complex business and legal environments in which they operate.

In the second tier are smaller exchanges; some regional, others national, and some serving specialised market segments such as the various commodities and futures exchanges. Among the second tier, for example, are found the Toronto Stock Exchange (TSX) in Canada, the OMX¹⁰ in the Nordic/Baltic region (now part of NASDAQ OMX), the ASX in Australia, and the KSX in Korea. Again, although roughly similar in size (that is to say, smaller than the big exchanges), each is very different in its own way. Nevertheless, these exchanges appear to punch above their weight. They have significance and play a role greater than their size might otherwise warrant, especially over the last decade or two. These second tier exchanges have been innovators, open to technology, quick to change and adept at seizing opportunities. Of course, not all experiments have been successful, as the demise of the Neuer Markt¹¹ demonstrates, and not all marriages are made in heaven, as the failed merger between the TSX and the LSE or between the ASX and Singapore attest. But these exchanges have been learning from each other, as well as innovating for themselves, creating models responsive to their particular circumstances.

Exchanges with British roots, such as the ASX, TSX and HKEx, have a long history of self-regulation. However, in different ways and in response to different pressures, each has moved sharply away from a self-regulatory model. Now potentially threatened by a move by NASDAQ into Canada, the TSX has long enjoyed national primacy in Canada. TSX itself was the result of the sudden consolidation of most of Canadian equity markets, and happily shed much of its regulatory role to focus on product innovation and its role as a national

¹⁰ OMX was formed by a progressive consolidation over time of a Swedish futures exchange with the Stockholm Exchange, the Copenhagen Exchange, and exchanges in Lithuania, Estonia, Latvia, Finland and Armenia.

¹¹ The Neuer Markt was the technology segment of the Deutsche Börse, which enjoyed success between 1997 and 2000. It imploded when the dot com bubble burst, and was eventually shut down in 2003.

marketplace. Its decisions were pragmatic, determined by competitive pressures from its large southern neighbour. Ironically, the lack of a federal securities regulator in Canada placed more pressure on the exchange itself to take measures to integrate market regulation on a nationwide basis.

Hong Kong's predecessor to HKEx relinquished most of its regulatory authority more reluctantly, only after years of skirmishes with a young regulator.¹² The resistance to realignment of regulatory authority in Hong Kong, however, could not withstand the combined pressures of the Asian financial crisis of 1997,¹³ the dramatic shift in regulatory authority in the UK (Hong Kong's model) from the LSE to the FSA in 2000,¹⁴ and the upsurge in Mainland Chinese listings.¹⁵ Until then, the longstanding potential for conflicts of interest, endemic in small financial communities such as Hong Kong, had not been sufficient, in and of itself, to prompt a major realignment of regulatory authority.

Australia's ASX, one of the first exchanges to demutualise,¹⁶ has trodden a more tortuous path in trying to delineate the boundaries of regulatory authority between exchange and government regulator. For many years after the demutualisation of 1998, the mechanisms designed to separate commercial and regulatory affairs within the exchange structure, as well as the relationship of exchange to regulator, were subject to constant rebalancing. This process of shedding self-regulatory authority by the exchange continues to evolve;¹⁷ the longstanding tentativeness of the situation in Australia, in part at least, appears to be a legacy of path dependency and political ideology as much as anything else. A merger with the Singapore Exchange would have vaulted ASX into the top of the Asia league tables,¹⁸ but that political joker, the national interest, as well as concerns over the dilution of government regulatory authority, derailed the transaction.

And then there are the rest, the small players and the sometimes not-so-small emerging, transitional or frontier markets, ranging from Johannesburg to Shanghai, from Jakarta to São Paulo, and from Bratislava to Bermuda. Some, like Johannesburg, have been around for a

¹² The Securities and Futures Commission (SFC) in Hong Kong was created in 1989, in response to the 1987 market crash, which shut the Stock Exchange of Hong Kong (SEHK) for several days.

¹³ Which gave government regulators the upper hand.

¹⁴ The UK market had long provided inspiration and technical expertise for Hong Kong.

¹⁵ Which prompted heightened regulatory concerns.

¹⁶ Number five, after Stockholm, Helsinki, Copenhagen, and Amsterdam.

¹⁷ For further details see Australian Stock Exchange, 'ASX Markets Supervision: New Structure to Operate from 1 July' (Media Release, 29 June 2006) <http://www.asxgroup.com.au/media/PDFs/mr20060629_asx_markets_supervision.pdf> accessed 3 October 2013.

¹⁸ See generally, 'Niche Markets and their Lessons' in Cally Jordan, *International Capital Markets: Law and Institutions* (Oxford University Press, 2014) ch 9.

long time; others are brand new (or recently resurrected from the ashes). Some, like Bermuda, are sophisticated, niche market players that hardly fit the profile of exchanges found in emerging economies. And others, like Jakarta, serve large, resource-based economies, where considerable pools of domestic capital vie with significant levels of political risk in shaping the markets.

That said, dramatic changes in modern capital markets are upsetting the established hierarchies among exchanges. In a remarkable resurgence, Sao Paulo soared from near oblivion to international prominence in scarcely a decade. China is a story unto itself; its domestic markets are unlike any others in the world, as are its regulatory approaches.

Traditional self-regulatory models are fading away (or were never embraced), a demutualised form is the new norm, consolidations appear more successful on a domestic or regional level than internationally and technological change is driving all. Everywhere, exchanges are under siege, rethinking their strategies and business model.

At this point, demutualisations¹⁹ and consolidations came to the fore, the one fuelling the other. The Stockholm Stock Exchange was the first to break ground in 1993. A wave of securities exchange demutualisations followed: Helsinki, Copenhagen, Amsterdam, the *Borsa Italiana*, the Australian Securities Exchange, Iceland, Athens, Singapore, the Singapore International Monetary Exchange (SIMEX) and the London International Financial Futures and Options Exchange (LIFFE), all demutualised before 2000.²⁰ After the deluge of demutualisations, exchanges began to transform themselves again through consolidation, in a process of ‘creative destruction’.²¹

The first major international consolidation was Euronext. On 22 September, 2000, the Paris, Brussels and Amsterdam exchanges came together in a new entity called Euronext.²² Others

¹⁹ Prior to exchange demutualisation, exchanges were held as ‘mutual’ associations – essentially non-profit and member-owned. With demutualisation, exchanges became shareholder held corporations and profit-maximizing business organizations. Thus, all exchange decisions were made by its members prior to demutualisation, including whom to admit as members. Post-demutualisation, shareholders influenced these decisions whether or not they were members.

²⁰ Benn Steil and André Meyer, ‘Why Do Exchanges Demutualize?’, *Mondo Visione* (online), 25 June 2002 <<http://www.mondovisione.com/exchanges/handbook-articles/why-do-exchanges-demutualize/>>. Not coincidentally, this wave of demutualisations coincided with a ‘bull market’ for equity securities and internationalisation of the markets, resulting in tidy profits for the exchange participants benefiting from the change in structure. Timing is all.

²¹ Shamshad Akhtar, ‘Demutualization of Asian Stock Exchanges – Critical Issues and Challenges’ in Shamshad Akhtar (ed), *Demutualization of Stock Exchanges: Problems, Solutions and Case Studies* (Asian Development Bank, 2002) 19. ‘In order to remain competitive, exchanges need to continually restructure and upgrade themselves based on the latest technological advancements in trading and information dissemination technology. Members of mutual exchanges have been unable or unwilling to commit to such investments. A profit-making exchange with transferable (and listed) shares would be able to access a broader investor base for such funds’.

²² Prior to its merger with the New York Stock Exchange, Euronext N.V. was a company domiciled in the Netherlands and was incorporated on July, 20, 2000 by Société de Bourses Françaises S.A. (SBF), Amsterdam Exchanges N.V. (AEX)

followed, the NYSE and Euronext in 2006 and the LSE and the *Borsa Italiana* in 2007. In the global waves of demutualisations, exchanges mimicked each other's organisational structures. Demutualisation had created a new dynamic among these exchanges.

II BASICS OF AN EXCHANGE

The exchange is a market place. Modern exchanges have usually combined three main functions: a trading system, a regulatory mechanism and operational systems,²³ all to a greater or lesser degree, depending on the exchange. The complexity of exchange structure and the ancillary functions they performed increased over time. Concentric circles of intermediaries and supporting service providers spun out from the exchange, intersecting with other existing private or public institutions.²⁴ Exchange members,²⁵ brokers and jobbers,²⁶ broker-dealers,²⁷ market makers, investment bankers, promoters, introducers,²⁸ advisers, credit institutions, depositaries, clearing houses, payment systems, identification systems,²⁹ – all of these proliferated. Internal and external regulatory mechanisms developed.

The forces of technology, competition and demutualisation³⁰ decoupled and realigned the traditional exchange functions of trading, regulating and operating. Exchanges are struggling to redefine themselves now and still make money through fee generation. Some exchanges

and Société de la Bourse de Valeurs Mobilières de Bruxelles S.A. (BXS). As at 22 September 2000, the three constituent companies merged into Euronext N.V.

With respect to Amsterdam, the merger was effected by means of a three-way legal merger between AEX, Euronext N.V. and its wholly-owned subsidiary Euronext Amsterdam N.V. In this merger, all assets and liabilities of AEX were transferred to Euronext Amsterdam N.V. and the shareholders and holders of profit-sharing certificates of AEX became shareholders of Euronext N.V.

On completion, all former shareholders of the Paris, Amsterdam and Brussels exchanges became shareholders of the holding company, Euronext NV, which in turn had, as wholly owned subsidiaries, the former three exchanges. Under the exchange ratio that was deployed, the former shareholders of SBF, AEX and BXS held, on completion, 60 per cent, 32 per cent and 8 per cent of the share capital of Euronext NV respectively.

²³ Jennifer Elliott, 'Demutualization of Securities Exchanges: A Regulatory Perspective' (Working Paper No WP/02/119, International Monetary Fund, 2002) 5-6.

²⁴ See also Jonathan R Macey and Maureen O'Hara, 'Globalization, Exchange Governance, and the Future of Exchanges' in Robert E Litan and Anthony M Santomero (eds), *Brookings-Wharton Papers on Financial Services* (Brookings Institution, 1999) 3. Five economic functions of exchanges have been identified: '1) liquidity, 2) monitoring of exchange trading against insider trading and manipulation, 3) standard-form, off-the-rack rules to reduce transaction costs for investors, 4) a signaling function to inform investors that the issuing company's stock is of high quality, 5) and a clearing function to ensure that secondary market participants receive cash for securities sold and timely delivery for securities purchased'.

²⁵ Prior to demutualisation.

²⁶ Before the 'Big Bang' in London; see Cally Jordan, *International Capital Markets: Law and Institutions* (Oxford University Press, 2014) ch 6.

²⁷ The US terminology for the major form of exchange intermediary.

²⁸ Various forms of intermediaries 'introduced' and monitored companies listing on an exchange, for example, the NOMAD of the London Stock Exchange. A NOMAD (nominated advisor) is a firm or company that the LSE licenses to manage new issuances to the AIM listing segment. It also acts as a de facto regulator.

²⁹ For example, CUSIP Numbers (Committee on Uniform Securities Identification Procedures): a CUSIP Number can be used to identify most securities for the purposes of clearing services.

³⁰ See discussion of demutualisation, above n 19.

have divested themselves or been relieved of their regulatory function; others have bulked up on a broader array of operational systems; even the trading function of exchanges is under threat from alternative trading systems. But exchanges continue to provide a nexus of market expertise, systems and information that can be put to new uses.³¹ Consolidations and alliances form part of their survival strategy.

As a market, exchanges used to be physical places. Most long established exchanges are still known by their place names (London, New York, Chicago, Tokyo, Toronto), although place has now become more or less irrelevant. As the financial products traded on exchanges dematerialised and diversified, electronic trading and virtual markets increasingly supplanted the physical exchange.³² New exchanges, such as ICE (Intercontinental Exchange), which has taken over NYSE-Euronext (and spat out Euronext), as well as Euronext itself, make no reference to their nominal country or place of origin. Older exchanges, such as the Chicago Mercantile Exchange too, rebranded themselves³³ Technology has permitted the disassociation of market from physical place; in theory, at least, there are now no practical impediments to cross-border or international exchanges and alliances. The reality, though, has proved more complex.

III FORMATIVE FORCES AND THE MODERN EXCHANGE

A Demutualisation

The popularity of demutualisation has been the key to formal merger and consolidation initiatives. The phenomenon of demutualisation, the change in form of exchanges from member-based associations (the exclusive country clubs of finance) to shareholder-based commercial entities, began some 20 years ago. It marked the beginning of a new era for exchanges, one that continues to unfold.

Exchanges are old institutions, the major ones predating the appearance of statutory business organisations, the corporation or registered companies. As a matter of practicality, they had assumed what over time became an increasingly archaic form of internal organisation. It is

³¹ For example, NYSE Euronext may assume responsibility for the management of the LIBOR rate setting system, which fell into disrepute under the aegis of the British Bankers Association. See NYSE Euronext, 'NYSE Euronext Subsidiary to Become New Administrator of LIBOR' (Press Release, 9 July 2013) <<http://www.nyse.com/press/1373365567815.html>>.

³² The physical trading floor of the London Stock Exchange, eliminated in 1986 is now represented by a spectacular hanging light sculpture in the atrium of its new premises in Canary Wharf.

³³ Now usually referred to by its holding company name, CME Group Inc.

somewhat ironic that one great motor of modern capitalism, the NYSE, would have been constituted for over a century³⁴ as a not-for-profit organisation under New York law. The exclusivity and privacy of the mutual association form appealed to the clubbish proclivities of the market intermediaries associated with exchanges, until outweighed by the opportunity, presented by demutualisation, to make a financial killing.³⁵

1 *The Exchange as Corporation*

By demutualising, an exchange changes organisational form to become a modern for profit business organisation, a corporation or shareholding company.³⁶ A mutually held and member owned exchange may choose to become a privately held corporation, thereby creating a share capital structure, but remaining member owned and controlled for all practical purposes.³⁷

Further private offerings can expand the shareholder base of an exchange, while retaining the benefits of private company ownership.³⁸ A variation on demutualisation makes shares publicly available although not listed, with caps or restrictions on voting so as to preserve original member control.³⁹ Finally, a demutualised exchange that lifts the trading restrictions on its shares can become fully publicly traded and list its shares to trade on exchange like any over corporation

³⁴ Until demutualisation in 2006.

³⁵ Pamela S Hughes, 'Background Information on Demutualization' in Shamshad Akhtar (ed) *Demutualization of Stock Exchanges: Problems, Solutions and Case Studies* (Asian Development Bank, 2002) 33, 33-34.

³⁶ See, Reena Aggarwal, 'Demutualization and Corporate Governance of Stock Exchanges' (2002) 15(1) *Journal of Application Corporate Finance* 105, 105-113: 'Traditionally, stock exchanges have been mutual associations owned by their members. Generally, they have been operated on a not-for-profit basis so that any profits are returned to members in the form of lower trading costs or access fees, but this has not always been the case.'

There are differences in the manner in which stock exchanges are operated and regulated. They differ in terms of the role of the board and the staff of the exchange, the powers of the chief executive and chairman and the composition and powers of exchange committees. Exchanges have a variety of voting structures and the balance of power between different users varies among them as well. ...

Perhaps the most distinguishing feature of the traditional stock exchange structure has been its cooperative governance model; the close identity between ownership of the organisation and the direct use of its trading services. The owners of the mutual enterprise are also its customers. Owner/customers may share in the net gains of the enterprise in proportion to their ownership interest. Decisions are usually made democratically, on a one member, one vote basis and often are made by committees of representatives of member firms.

The ability to influence the decisions of the exchange is thereby separated from the level of economic interest a member has in the exchange. Ownership rights may not be freely tradable or exchangeable and on cessation of membership, those rights are forfeited. Because the organisation's constituting documents may expressly (or impliedly) adopt a non-profit objective and prohibit the distribution of surpluses, mutually owned exchanges are seldom able to raise capital from anyone other than their members.'

³⁷ For example, the London Stock Exchange in 1986. London Stock Exchange, *Our History* (7 July 25) <<https://web.archive.org/web/20150905191913/http://www.londonstockexchange.com/about-the-exchange/company-overview/our-history/our-history.htm>>.

³⁸ Aggarwal, above n 36, 107.

³⁹ See: Ibid, a typical restriction is to limit ownership or voting rights for any one shareholder to 5%.

The twist here is whether the exchange lists its shares on its own listing platform, thereby creating potential conflicts of interest.⁴⁰ With the exception of this last twist, the choices and organisational permutations available to a demutualised exchange are not very different from those open to any other business entity with a share capital structure. As with any other corporation, there is no inevitability about this linear trajectory from mutual association to publicly listed corporation. Some exchanges demutualise immediately into fully-fledged publicly listed corporations (such as the Bolsa Mexicana).⁴¹ And, like any other corporation, profit maximisation to the benefit of shareholders becomes their reason for being.

Interestingly, very little attention has been paid to the implications of use of the corporate form itself by an exchange.⁴² In the United States, the corporate form does mean that a listing will trip numerous triggers designed to increase transparency and reduce conflicts of interest: insider trading regulations, extensive disclosure and other issuer regulation. The debate surrounding demutualisation of the NYSE in 2006, for example, noted that demutualisation would address the opaqueness of the member association form and perceived internal governance abuses. Adoption of the corporate form potentially extends the reach of external regulation applicable to the exchange.

Compared to the United States, corporations law in continental Europe is prescriptive and quite regulatory to begin with. There are still minimum capital requirements for commercial corporations, as well as more structured and mandatory internal corporate governance mechanisms. Corporate law in Europe demonstrates a greater degree of public interest (workers councils or workers representation in dual board structures, for example). There is little of the balancing of external regulation against self-regulatory functions. In Europe, the regulators regulate.

The concept of the independent, privately-funded, self-regulatory organisation is somewhat alien in continental Europe. Regulators may not be as close to the market, but many believe there is vigorous regulatory oversight. For an exchange to adopt corporate form is seen as a

⁴⁰ The conflict of interest arises due to the dual capacities in which the exchange is operating; as an exchange it is engaging in decision-making as to its operations which may affect its listed companies. The danger lies in the potential for self-interested decision-making favouring the exchange itself in its capacity as a listed company.

⁴¹ See 'Stock Exchanges – An Endangered Species' in Cally Jordan, *International Capital markets: Law and Institutions* (Oxford University Press, 2014) ch 10.

⁴² Euronext, *Form S-4 Registration Statement* (21 September 2006) <http://www.sec.gov/Archives/edgar/data/1368007/000104746906011989/a2173235zf1_s-4.pdf>. The merger of NYSE and Euronext focused on the significance of the use of the corporate form. Each of the NYSE and Euronext proposed the creation of non-corporate entities (in the case of Euronext, a Dutch foundation, and NYSE, a Delaware trust) to which shares of the ultimate holding company would be transferred in the event of untoward regulatory actions that might otherwise catch the holding company and result in 'regulatory creep'.

fairly non-contentious move, with little internal resistance from self-interested parties chary of losing autonomy. It also means that the exchange becomes subject to the real strictures of corporate law. Euronext, for example, was formed as a Dutch limited liability company with a two-tier board structure (arguably providing a superior form of internal governance than the Anglo-American single board structure). In addition, Euronext triggered oversight by multiple regulators, the Dutch Ministry of Finance, the French *Autorité des marchés financiers*, various interagency memoranda of understanding and EU Directives (to name a few sources of external regulatory pressure and oversight).

Share ownership restrictions, implemented to deter self-interested behaviour on the part of a dominant shareholder, also appear in demutualised exchanges.⁴³ Such restrictions already exist in some European corporate laws and some Commonwealth banking laws. The more cynical might see such restrictions as a form of protectionism, deterring foreign control of a national symbol.

The substantial differences in national corporate laws may result in persistent differences in internal and external governance of demutualised exchanges and the extent of government regulatory intervention. There are other intriguing implications for exchange structures. Because United States corporate law is enabling and non-regulatory in nature, the NYSE found itself creating compensatory internal governance measures when demutualising. Some of these compensatory mechanisms, such as the dual board structure and a chief regulatory officer reporting to a regulatory committee rather than the CEO,⁴⁴ were directly or indirectly inspired by European corporate law. In a further twist, the NYSE and Euronext, in their merger, employed associated non-corporate law vehicles (a Delaware trust and a Dutch foundation) as an escape hatch if unwelcome regulatory triggers were tripped in the future.

2 Implications of Demutualisation

Demutualisation brings benefits, at least in theory: better corporate governance mechanisms, the possibility of raising capital without admitting new operational members to the exchange itself and more flexible structuring of exchange alliances and formal mergers.⁴⁵ A

⁴³ See Aggarwal, above n 36, 107, see the for-profit private company stage, and following stages, above in Aggarwal's five stage demutualisation process.

⁴⁴ Roberta Karmel, 'Government Regulatory Intervention in the Governance of Market Infrastructure Institutions' (2006), working paper in the author's possession.

⁴⁵ For a more comprehensive discussion of the benefits of demutualisation, see Richard A Grasso (Chairman, NYSE), 'Testimony before Committee on Banking, Housing and Urban Affairs', U.S. Senate regarding Public Ownership of the U.S. Stock Markets (28 September 1999).

demutualised exchange, especially a publicly traded one acquires a ‘merger currency’, its shares.

In a mutual exchange, members are owner operators. Members, usually brokers, tended to close ranks and in the absence of open corporate governance practices designed to promote accountability and organisational renewal, became attached to their old ways.

Brokers inadvertently resisted changes if these entailed additional costs, loss of revenue or competitive threat. This resistance eventually impeded the ability of the company to react quickly to a rapidly changing market environment.⁴⁶

Demutualisation resulted, to a greater or lesser degree, in a formal separation of ownership and management.

Exchanges are also subject to external oversight in most cases, given their public interest function. Other governance mechanisms may overlay the usual ones associated with corporate form, such as public ‘fit-and-proper’ screenings and regulatory reports by the board and management.⁴⁷

Demutualisation can also lead to the admission of a greater number of trading partners. When the country club of existing members decides to grant trading rights to a new party under a mutually held organisation, they effectively must give that party equity in the exchange (to be consistent with the mutual form).⁴⁸ Members may attempt to protect their territory and be disinclined to admit many (or any) new partners. The demutualised corporate form solves that problem. Exchanges become much more likely to extend trading rights to new participants, as that can lead to beneficial effect on profits and exchange value.⁴⁹

Demutualisation makes structuring alliances and formal mergers with other exchanges easier. The same competitive forces that push exchanges to demutualise and reinvent themselves demand that exchanges form alliances with other exchanges. The incentives built into mutually held organisations are woefully inadequate in this respect.

Factionalisation is always a risk in mutual exchanges, fracturing the exchange along lines of interest. Fearing the disproportionate impact of a merger on trading activity, smaller members of an exchange may oppose it. In contrast, a demutualised exchange with a board and management accountable to shareholders will seek profit-generating alliances.

⁴⁶ Akhtar, above n 21, 12.

⁴⁷ Ibid 13.

⁴⁸ Ibid 14.

⁴⁹ Ibid.

Demutualisation facilitates friendly mergers and alliances by providing the currency for the transaction, through share exchanges and new issuances. But publicly traded shares also open the door to hostile takeover bids. The City of London expressed its indignation when the London Stock Exchange found itself, several times, assailed by unwelcome suitors, such as the upstart OMX or later by NASDAQ.

Demutualisation also brings problems, primarily conflicts of interest created or intensified by the profit motive, as well as with respect to rule-making and self-listing arrangements. The concern is ‘whether the commercial pressures [or governance structure] of a for-profit entity will undermine the commitment of resources and capabilities of the exchange to effectively fulfil its regulatory and public interest responsibilities to an appropriate standard’.⁵⁰

Demutualisation intensifies the conflicts of interest inherent in self-regulation to the extent exchanges retain such powers. A demutualised exchange must balance profit generation and the promotion of business opportunities against its role in supporting the ‘integrity and efficiency of capital markets by setting and enforcing appropriate rules to regulate its market’.⁵¹ A traditional exchange assumes a number of different responsibilities, including devising rules for trading and ensuring that they are observed, determining qualifications for listing or admission to trading, and conducting surveillance of the market and its participants, investigating violations, and disciplining violators.⁵² Demutualised exchanges may be reluctant to spend adequate resources on regulation and may not be willing to enforce rules against themselves or participants who bring in large volumes of trading or liquidity.

The quandary created by exchanges listing their own shares on themselves is simple enough. However, such an arrangement presents a novel conflict of interest. IOSCO expressed the concern that ‘the market disciplines on proper behaviour may not be strong enough where the exchange is being asked to regulate its own listing’.⁵³ Generally though, even if an exchange’s securities are only admitted to trading on its own market, some of the potential conflicts may be lessened if a third party regulates the trading of that exchange’s securities.

⁵⁰ Commonwealth, *Parliamentary Debates*, House of Representatives, 27 November 1997, pg 11541 (Chris Miles). From the speech presenting legislation authorising demutualisation of the Australian Stock Exchange.

⁵¹ Frank Donnan, ‘Self-regulation and the Demutualisation of the Australian Stock Exchange’ (1999) 10 *Australian Journal of Corporations Law* 1.

⁵² *Ibid.*

⁵³ Technical Committee, International Organization of Securities Commissions (IOSCO), ‘Issues Paper on Exchange Demutualization’ (IOSCO, 2011) 9 <<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD119.pdf>>.

Demutualisation, as much as it has been a catalyst for consolidation of exchanges (willing or not), can also throw up barriers. The best laid plans of directors and managers may be scuppered by pesky shareholders, as the Deutsche Börse board learned to its chagrin in its merger talks with the London Stock Exchange in December 2004. And not all exchanges have rushed into demutualisation, for various reasons. They may be able to afford their clubbiness and view a formal merger or consolidation as dilution of their brand (as did New York and London, at various times, or the Swiss exchanges). One of the many impediments to the creation of a ‘China Stock Exchange’ is the old-fashioned ‘mutualised’ form of Shenzhen and Shanghai, compared to the slick, very with it, demutualised HKEx.

B Technology and Globalisation

The twin forces of technology and globalisation are commonly credited with revolutionising securities trading and the exchanges, in particular.⁵⁴ Floor trading involved traders shouting out bids ‘in the pits’, aided by arcane hand signals. Despite the ‘fear and loathing’ with which electronic trading was greeted by some old-timers, it has rendered floor trading virtually obsolete.⁵⁵

Trading has now become divorced from geographic place, and possibly regulatory reach, which remains territorially based; trading is in the cloud. Trades take place at lightning speed, exponentially increasing potential trading volume, liquidity and volatility, as well as the potential for disastrous error.⁵⁶ In addition to the ‘fat finger’ effect attributed to human error, the robustness of the systems themselves to handle the new trading patterns is a serious and growing concern, the consequences of which may be seriously underestimated.⁵⁷ Magnitude may exacerbate the vulnerability of modern trading technology, making bigger exchanges which straddle time zones and regulatory boundaries, more susceptible to market failures. As the regulatory net tightens, freewheeling cross-border exchange activity may be reined in.

⁵⁴ See Ruben Lee, ‘Changing Market Structures, Demutualization and the Future of Securities Trading’ (Working Paper, 5th Annual Brookings/IMF/World Bank Financial Markets and Development Conference, 15 April 2003) [unpublished]: “It is widely recognized that the pressures of competition, globalization, and technological change, are threatening the development, and in some instances the very survival, of many developing capital markets.” See also Ruben Lee, *Running the World’s Markets: The Governance of Financial Infrastructure* (Princeton University Press, 2011); There are, however, many more sources in the literature affirming this principle.

⁵⁵ Jack Farhy, ‘End of an Era as LME is Sold for £1.4bn’, *Financial Times* (online), 25 July 2012 <<http://www.ft.com/intl/cms/s/0/1db65672-d668-11e1-bd9c-00144feabdc0.html?siteedition=intl&siteedition=intl#axzz2gCk5Phsy>>.

⁵⁶ The so-called ‘fat finger’ mistakes, where a slip of a finger on a keyboard can throw markets into free fall.

⁵⁷ For example, the SEC has recently fined NASDAQ OMX for system failures associated with the debacle of the highly publicised Facebook initial public offering. See Arash Massoudi, ‘Nasdaq Prepares for \$10m SEC Fine Over Botched Facebook IPO’, *Financial Times* (online), 24 April 2013 <<http://www.ft.com/intl/cms/s/0/a39fb2ee-acd5-11e2-b27f-00144feabdc0.html#axzz2gCk5Phsy>>.

Technology requires new skills and breeds new industries and players. The acquisition of technology itself has motivated some consolidations as well as providing alternatives to formal mergers. NASDAQ has been successful in commoditising its trading platform technology, turning it into a revenue generating business. Compatible trading technology is obviously an attractive feature to potential merger partners (such as was the case with Singapore and Sydney). But compatible trading platforms can also link exchanges through alliances that stop short of formal merger or consolidation. The Shanghai-Hong Kong Stock Connect comes to mind.

New forms of organisation, together with alliances that might not have been imaginable in even the recent past, have transformed exchanges, sometimes in unexpected ways. For example, the Amsterdam Exchange, seeking flexibility and competitive advantage demutualised then merged with Paris and Brussels to form a new regional exchange, Euronext. The NYSE then rolled Euronext into the gargantuan transatlantic exchange, NYSE-Euronext, which Atlanta-based ICE then swallowed,⁵⁸ spitting out Euronext in the process.⁵⁹ The Amsterdam Exchange, its best laid plans having gone awry, appears to have sunk into oblivion, with its talent moving away to high frequency trading centres scattered around Amsterdam.⁶⁰

Globalisation has increased pressures on exchanges to find new strategies, and sometimes, new partners. Financial centres to be reckoned with have multiplied, in a process dubbed ‘multipolarity’,⁶¹ Hong Kong, Singapore, Kuala Lumpur, for example.⁶² These rising regional centres place competitive pressures on the established exchanges. The closed cells of finance, and the cosy clubs, have burst open. ‘The traditional exchange governed by its members is seen to be unable to adequately respond to competitive pressures – a governance structure that relies on member decision making is slow and encumbered by the many, and often

⁵⁸ Jacob Bunge, ‘SEC Approves ICE-NYSE Deal’, *Wall Street Journal* (online), 16 August 2013 <<http://online.wsj.com/article/SB10001424127887323639704579016521606693810.html>>.

⁵⁹ Ibid.

⁶⁰ ‘Dutch Fleet: The Home of the World’s First Stock Exchange is Now a High-Frequency Heartland’, *The Economist* (online), 20 April 2013 <<http://www.economist.com/news/finance-and-economics/21576423-home-worlds-first-stock-exchange-now-high-frequency-heartland-dutch>>.

⁶¹ See Nicholas Véron, Guntram B Wolff and Jacob Funk Kirkegaard (eds), *Transatlantic Economic Challenges in an Era of Growing Multipolarity* (Bruegel Institute, 2012).

⁶² See also the case study on the Bolsa Mexicana in this chapter. The Bolsa Mexicana demutualised to raise capital, which it committed to consolidating its businesses and improving the technology of the trading platform it runs. The Bolsa’s demutualisation, IPO and subsequent performance illustrates a securities exchange that is competing to remain technologically up to date, trying to find a niche (through its derivatives alliance with the Chicago Mercantile Exchange), and which is trying to remain regionally relevant (exploring the possibility of a pan-Latin American alliance, MILA). For more on MILA, see Philippe Carré, ‘Comment: Pan-Latin American Exchange in Sight?’, *Financial Times* (online), 10 January 2010 <<http://www.ft.com/intl/cms/s/0/72a33da4-3b71-11e1-a09a-00144feabdc0.html#axzz2X6TTymy5>>.

conflicting, interests of the individual members’.⁶³ Demutualisation was an early, but perhaps ultimately inadequate, response.

Technology and globalisation have eaten away at the traditional business model of established exchanges. ‘Trading has become global as the role of the exchange has become less relational’.⁶⁴ No more long lunches needed. Additionally, the cost of information, once to the advantage of a domestic exchange, has plummeted.⁶⁵ Exchanges have sought growth and revenues through diversification, new product lines, new businesses; consolidations promise, although they do not necessarily deliver, reduced costs, economies of scale and more varied revenue streams. It is easy to see how the dream of a ‘global exchange’ to channel these forces has arisen. Nevertheless, the dream has not materialised to date; structural impediments, such as ‘silos’ and incompatible business strategies, often stymie consolidation efforts.

The swing away from autonomous, self-regulatory, exchanges has also played into the ‘commoditisation of exchange trading’. Regulators, from the SEC and the CFTC in the United States to the European Commission⁶⁶ and the new European regulator, ESMA, are reshaping the exchanges, but now in a very public, and potentially less idiosyncratic, way. Regulatory catch-up and convergence over the long term (and perhaps the very long term) may facilitate cross border consolidations, in China for example.

According to O’Hara and Macey, of the five economic functions usually associated with exchanges,⁶⁷ only liquidity remains. So the fight is over liquidity. Exchanges need the capital to keep up with changing technology to promote trading volume and the flexibility to create global alliances, to the same end. These alliances invariably gravitate to the epicenter of economic growth. In sum, globalisation giveth whereas technology and regulation taketh.⁶⁸

Technology has been racing ahead of markets and regulators alike, blithely ignoring national boundaries and concepts of jurisdiction. The implications are profound. Until the new normal emerges to provide some modicum of stability and predictability to market developments,

⁶³ Elliott, above n 23, 8.

⁶⁴ Macey and O’Hara, above n 24, 2-3.

⁶⁵ Ibid.

⁶⁶ Which is currently developing the MiFID 2 regime.

⁶⁷ Macey and O’Hara, above n 24.

⁶⁸ ‘[E]xchange births are positively correlated with economic growth and commodity booms, while closures are associated with advances in communications technology, such as telephone and the Internet, and heightened regulation, such as the 1934 Securities Exchange Act and state-level blue sky laws in the United States and the 1963 Stock Transfer Act in the United Kingdom’; See Bjorn N Jorgensen, Kenneth A Kavajecz, and Scott N Swisher IV, ‘The Historical Evolution of Financial Exchanges’ (September 4, 2011) <<http://ssrn.com/abstract=1922250>>.

regulators and exchanges are engaging in unprecedented market interventions, scrambling to apply quick fixes.

C The Courting Game: Exchange Consolidations

Freed by technology from the imperatives of geography and facilitated by demutualisation, exchanges set about hunting for liquidity and competitive advantage through regional and international alliances, partnerships, joint ventures and formal mergers. Survival was at stake, and to survive they had to make a profit. 'No matter how often stock exchanges say they are capital-raising venues, and futures exchanges say they are risk-management venues, the bottom line in a profit-driven model is: anything that generates more trading and speculative activity is going to generate more commercial activity for them'.⁶⁹

As technology and competition drove down trading costs, resulting in diminished fee generation, and capital raising shifted from public to private markets, exchanges have looked to diversify across product lines and services. Jurisdictional restraints, especially regulation in the United States, made international alliances and partnerships attractive. Small exchanges, seeking to avoid irrelevancy, overcame longstanding historical and political rivalries, to join forces.⁷⁰ To remain competitive, exchanges began reorganising themselves in response to economic conditions, the size of other exchanges, in recognition of their particular niche. And, profit-maximising entities tend to seek growth.

The phenomenon of cross-listing, whereby companies expanding operations internationally list their securities on several exchanges, tempts exchanges to consolidate so as to increase efficiency of trading and profit.⁷¹ If providing liquidity is now the primary economic function of an exchange, then the market that can provide the most liquidity will be the most competitive. That market will also be the largest. Or so the theory goes.

The last decade has seen an on-going game of courtship and conquest, as exchanges realign, reconfigure, and retrench. Several basic categories of consolidation have been helpfully identified, although some have spent their force and newer variations continue to appear.

⁶⁹ Jeremy Grant, 'A Market to Capture', *Financial Times* (online), 17 February 2011 <<http://www.ft.com/cms/s/0/11c61144-3aca-11e0-9c1a-00144feabdc0.html#ixzz2VxuCEkza>>.

⁷⁰ Euronext, for example. Another example would be the Baltic and Nordic exchanges, which have come together under the NASDAQ OMX Group, including Copenhagen Stock Exchange, Riga Stock Exchange, Icelandic Stock Exchange, and Armenian Stock Exchange.

⁷¹ Susan Wolburgh Jenah, 'Commentary on: A Blueprint for Cross-Border Access to U.S. Investors: A New International Framework' (2007) 48 *Harvard International Law Journal* 69.

Table 1: Types of exchange consolidation⁷²

Type	Summary
Domestic merger	Two or more domestic exchanges merge into a single national exchange, which could attract foreign investors.
Regional/global merger	Two or more domestic or regional exchanges (trading the same securities) merge into a regional exchange.
Vertical integration	A single exchange takes ownership of clearing, settlement and depository institutions.
Niche integration	Exchanges trading in specific securities, such as derivatives, merge into a niche regional or global exchange for that particular security.

Many domestic mergers have run their course.⁷³ By achieving economies of scale and perhaps attracting foreign investors due to their critical mass, they produced cost-saving benefits for the exchanges. However, domestic mergers inevitably raised issues of reduced competition leading to monopolistic behaviour⁷⁴ which persists until routed by either a new domestic trading venue (exchange or not) or foreign rivals poaching domestic listings. In the United States, the latest iteration of this trend was the acquisition of NYSE Euronext by ICE. Euronext was spun off, leaving the the two domestic US exchanges as affiliates, the NYSE now a subsidiary in the Atlanta-based ICE empire. Because exchanges in the United States are regulated separately along product lines (ie cash equities, futures, commodities and derivatives), the exchanges themselves cannot merge across these product lines.

Regional mergers quickly followed domestic consolidations. These supra-national exchanges can become very large, achieving economies of scale. Since the trading infrastructure has been the biggest fixed cost of an exchange, the cost to the exchange per trade decreases as more trades are executed on its platform. At least, that was the thinking. NYSE-Euronext in its heyday executed 7 million derivatives contracts per day.⁷⁵ Trading fees and commissions could be lowered, but high volumes of trading would be required; only mega-exchanges, it was thought, could achieve this.

⁷² Akhtar, above n 21, 16-18.

⁷³ The acquisition of the NYSE by ICE is a new development.

⁷⁴ Akhtar, above n 21, 18.

⁷⁵ NYSE Euronext, 'NYSE Euronext Announces Trading Volumes for April 2013' (News Release, 7 May 2013) <<http://www.nyse.com/press/1367834502271.html>>.

In the heady days of internationalisation of markets prior to the global financial crisis, the benefits of regional and global mergers on an exchange's profits were perceived to be so great that some even foresaw a future populated by a few global exchanges.⁷⁶ The NYSE-Euronext, the proposed MILA exchange in Latin America, and the NASDAQ-OMX merger, all suggested that the future was now. However, the breakup of NYSE-Euronext, the inability of any exchange (except Milan) to merge with the LSE,⁷⁷ the failure of or disinterest in exchange mergers in the Asia-Pacific, also suggest that geopolitical, historical and other economic obstacles persist.

Consolidation can take forms other than formal mergers across exchanges. An exchange can consolidate activities through vertical and horizontal integration of services and products. An excellent example of vertical integration is the Bolsa Mexicana de Valores (BMV) initial public offering. Prior to the offering, the BMV held equity in several ancillary service providers. By consolidating these services and bringing everything in-house, the BMV has been able to streamline its business, lowering costs. Additionally, the consolidation provides the BMV with alternative sources of revenue, which offset unexpected drops in trading volume.

However, vertical integration can become a source of conflict in other merger contexts. For example, during the failed LSE-Deutsche Börse merger, the issue of choice of clearing and settlement system arose. The Deutsche Börse owned Clearstream, a clearinghouse, as part of its vertical "silo"; the LSE had arrangements in place with London Clearing House, which was owned by a third party.⁷⁸ In theory, where trades are cleared and settled should be a clerical matter of little significance. However, the tight integration of clearing and settlement within the Deutsche Börse structure left the LSE vulnerable in case of disagreement with its future partner. While the issue was not pivotal in that case, it demonstrates non-economic factors that can affect the success or failure of a proposed merger.

Finally, niche integration has the benefit of attracting investors interested in a specific financial product. Identification of an exchange with that product will lead to concentration of the market, greater trading volumes and, again in theory, cost efficiencies and better price

⁷⁶ See 'Battle of the Bourses', *The Economist* (online), 25 May 2006 <<http://www.economist.com/node/6978712>>.

⁷⁷ For a chronology of the many attempts to merge with the LSE, see 'London Stock Exchange's Tumultuous History of Bids', *The Telegraph* (online), 2 September 2011 <<http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/8311679/London-Stock-Exchanges-tumultuous-history-of-bids.html>>.

⁷⁸ Jane Martinson, 'We Won't Sell Clearstream to Win LSE, Say Germans', *The Guardian* (online) 4 January 2005 <<http://www.guardian.co.uk/business/2005/jan/04/1>>.

discovery. Consequently, some exchanges specialise in certain types of securities. For example, the Toronto Stock Exchange (TSX) attempts to attract equities in specific sectors: mining, energy, and clean technology.⁷⁹ Creating an index for energy companies listed on the TSX, such as the S&P/TSX Capped Energy Index, signals the expertise and specialisation to investors.

Another good example of niche integration is the CME-BMV alliance. Prior to its demutualisation and initial public offering, the BMV held a monopoly on Mexican derivatives trading, through its MexDer platform. After demutualising, it sought a way to expand its derivatives business. By linking up with the Chicago Mercantile Exchange (CME), the largest futures exchange in the United States, MexDer was able to extend its global reach. Jorge Alegría, MexDer's CEO, stated:

This is very important for us because it is essentially an alliance with the biggest exchange in the world. It will enable us to connect our derivatives market with that exchange, and that will allow us to achieve much more liquidity and increase our capacity to distribute our products globally.⁸⁰

The alliance allowed BMV and CME investors to trade in the other's securities without opening two accounts. The CME already had a similar arrangement with Brazil's BM&F Bovespa, meaning that BMV investors tapped into a pan-Americas derivatives market through their own exchange.

Technology has been racing ahead of markets and regulators alike, blithely ignoring national boundaries and concepts of jurisdiction. The implications are profound. Until the new normal emerges to provide some modicum of stability and predictability to market developments, regulators and exchanges are engaging in unprecedented market interventions, scrambling to apply quick fixes.

⁷⁹ TMX, *Sector Profiles – Energy* <http://www.tmx.com/en/listings/sector_profiles/energy.html>.

⁸⁰ Jeremy Grant and Adam Thomson, 'CME Agrees to Bolsa Mexicana Alliance', *Financial Times* (online), 8 March 2010 <<http://www.ft.com/intl/cms/s/0/db13e39c-2adf-11df-886b-00144feabdc0.html#axzz2XIYtEcTc>>.

Part A The Big Deal- NYSE-Euronext

A.1 EURONEXT – MADE IN EUROPE*

I INTRODUCTION

On September 22, 2000, the Bourse de Valeurs Mobilières de Bruxelles SA ('BSX'), Société de Bourses Françaises SA ('SBF') and Amsterdam Exchanges NV ('AEX') engaged in a merger, creating Euronext NV.¹ In doing so, these parties gave rise to the first multinational exchange operator in Europe,² which would eventually provide a single trading platform for securities trading on a pan-European scale. Euronext NV was joined by the London International Financial Futures and Options Exchange ('LIFFE') in 2001,³ and the Portuguese exchange, Bolsa de Valores de Lisboa e Porto ('BVLP') in 2002.⁴

This chapter provides an account of the evolution of the Euronext exchange from the time of its inception, through to its merger with the New York Stocks Exchange in 2007.⁵ It discusses the factors which provided the grounding for the Euronext merger, the reasons for which the Euronext exchange came together, the trading platforms and regulatory oversight involved with the exchange, and the effects of the merger on the constituent exchanges.

The first section discusses the economic and regulatory factors specific to the European market, which led to a desire for a consolidation of securities exchanges. The second section explains the structure of the Euronext trading platform and regulatory oversight, and how both of these evolved between 2000 and 2007. Finally, the third and last section discusses the effects of the Euronext consolidation on the participating securities exchanges.

II THE EVOLVING EUROPEAN MARKET

The emergence of Euronext was not an isolated incident, but rather a symptom of rapid growth in international capital flows beginning in the 1960s and exponentially increasing in

* The author would like to acknowledge, in particular, the assistance of James Szauer and Brendan Donohue with this chapter.

¹ Euronext, *Brussels* <<https://www.euronext.com/en/markets/nyse-uronext/brussels>>.

² Euronext, 'Annual Report 2001' (Company Report, 2001) <http://www.zonebourse.com/EURONEXT-16725768/pdf/6917/EURONEXT_Rapport-annuel.pdf>.

³ 'Liffe Chiefs Back Euronext Bid', *BBC News* (online), 29 October 2001 <<http://news.bbc.co.uk/2/hi/business/1626392.stm>>.

⁴ 'BVLP Joins Euronext', *Mondo Visione* (online), 30 January 2002 <<http://www.mondovisione.com/news/bvlp-joins-uronext/>>.

⁵ See, Phillipa Leighton-Jones and Luke Jeffs, 'The Road to Consolidation – An Exchange Merger Timeline', *Financial News* (online), 15 February 2008 <<http://www.efinancialnews.com/story/2008-02-15/the-road-to-consolidation-an-exchange-merger-timeline-1>>.

the 1980s and 1990s.⁶ As investor demand rose around the world for international capital and portfolio diversification, securities began to be traded in increasing volumes across borders. In response, domestic securities exchanges set their sights to meeting this demand by internationalising and changing their legal status from mutual associations to demutualised companies limited by shares.⁷ This dramatic change in direction and legal status meant that securities exchanges became profit-driven market actors, and as such, were in direct competition with one another, and could both merge and issue securities of their own.

Amid these dramatic shifts in the global securities markets, the European Union ('EU') pursued a drastic course of development in economic governance. Most notably, it attempted to solidify its fiscal unity by launching the Euro in 1999.⁸ Further, it pursued a determined course toward integration of financial markets and its regulation,⁹ firstly through the Financial Services Action Plan ('FSAP') in 1999, and subsequently through a series of key directives which implemented the FSAP.

These conditions cumulatively provided the conditions for the creation of Euronext. This section discusses the economic and regulatory conditions relevant to the merger in more detail, and concludes by discussing the reasons given by the founding members of the market for its inception.

A Economic and Political Factors

It has frequently been noted that European stock markets were 'underdeveloped' when compared to US markets, particularly in the area of retail equity trading.¹⁰ However, on closer analysis, the European markets and the United States' markets were simply different. Certainly, there was a history of disinterest in retail trading markets in Europe; in the lead up to the Euronext merger, the securities markets in Europe were about half the size of their American counterparts.¹¹ Despite this, there were several important economic strengths of the

⁶ Martin D D Evans, 'International Capital Flows and Debt Dynamics', (Working Paper No WP/12/175, International Monetary Fund, July 2012), 3 <<https://www.imf.org/external/pubs/ft/wp/2012/wp12175.pdf>>.

⁷ Joseph A Grundfest, 'Internationalization of the World's Securities Markets: Economic Causes and Regulatory Consequences' (1990) 4 *Journal of Financial Services Research* 349.

⁸ Bill Lucarelli, *Endgame for the Euro: A Critical History* (Palgrave Macmillan, 2013) 89-101.

⁹ NYSE Euronext, 'Amendment No. 1 to Annual Report on Form 10-K for the Fiscal Year Ended December 31 2006' (Commission Filing, No 001-368007, Securities and Exchange Commission) 50 ('Amendment No. 1').

¹⁰ See, eg, Rafael La Porta et al, 'Legal Determinants of External Finance' (1997) 52 *The Journal of Finance* 1131; Rafael La Porta et al, 'Law and Finance' (1998) 106 *Journal of Political Economy* 1113; Katharina Pistor, 'Law in Finance' (2013) 41 *Journal of Comparative Economics* 311.

¹¹ Alexandre Lamfalussy et al, 'Final Report of the Committee of Wise Men on the Regulation of European Securities Markets' (Committee Report, European Union's Economic and Finance Ministers (ECOFIN), 15 February 2001) 10.

European market which contributed to the appeal of the Euronext merger, quite separate from the political and regulatory push toward market convergence.

First and foremost, the implementation of the Euro common currency in 1999 signified an economic movement toward convergence of the financial systems of those EU Member States which signed the Maastricht Treaty in 1992.¹² As a growing number of countries adopted the Euro (last count, 19),¹³ intra-country currency exposure¹⁴ diminished greatly.¹⁵ This means that European investors, which may previously have been heavily influenced by home bias would be less inclined to limit their investment to their home country and would, at least within Europe, invest more actively across borders.

Secondly, though the equity culture in Europe was historically been weak compared to the US, it took a dramatic turn for the better around the turn of the century, when the Euronext parties were seeking to converge.¹⁶ Whereas European investors had previously deposited their savings in what they termed to be ‘safer’ investments like bank accounts or real estate, they were increasingly turning to equity investment as a means of growing and preserving their wealth. For example, in the UK in 1980 only one in ten households were estimated to hold shares directly, which was significantly different to the one in five households in 1990.¹⁷

A last, more political, factor which inhibited, rather than promoted securities market integration in Europe was the tendency of European states to hold steadfastly onto their exchanges as national symbols.¹⁸ As securities exchanges had existed throughout Europe for hundreds of years, a visible centre of commercial activity, there was some sentiment attached to the institutions.¹⁹ However, as dematerialisation took hold, and eventually extinguished the physical stock exchange,²⁰ this concern became less pronounced. However, by this stage the damage had been done and the impediments to consolidation had solidified. These impediments were set out by McAndrews and Stefanadis in 2002.²¹ Firstly, pre-merger,

¹² *Treaty on European Union*, Belgium, Denmark, Germany, Greece, Spain, France, Ireland, Italy, Luxembourg, The Netherlands, Portugal, United Kingdom, signed 7 February 1992, OJ (entered into force 1 November 1993).

¹³ European Union, *The Euro* < http://europa.eu/about-eu/basic-information/money/euro/index_en.htm >.

¹⁴ The risk associated with an unexpected change in exchange rates.

¹⁵ James McAndrews and Chris Stefanadis, ‘The Consolidation of European Stock Exchanges’ (2002) 8(6) *Current Issues in Economics and Finance* 1, 1.

¹⁶ *Ibid*, 2.

¹⁷ James Banks and Sarah Tanner, ‘UK Household Portfolios’ (Working Paper No 00/14, Institute for Fiscal Studies, April 2000) 25.

¹⁸ Cally Jordan, *International Capital Markets: Law and Institutions* (Oxford University Press, 2014) 255.

¹⁹ For example, the Amsterdam stock exchange can be said to have existed since the Dutch East India Company established a market upon which it sold printed stocks and bonds in 1602.

²⁰ Stijn Claessens, Thomas Glaessner and Daniela Klingebiel, ‘Electronic Finance: Reshaping the Financial Landscape Around the World’ (2002) 22 *Journal of Financial Services Research* 29, 30, 36-42.

²¹ McAndrews and Stefanadis, above n 15, 3-4.

investors stood to benefit from ‘product differentiation’ which means that they could purchase various different financial products being offered in discrete smaller exchanges in an attempt to diversify their securities portfolios, a benefit which stood to be lost with a merger of exchanges. Secondly the legal and regulatory differences throughout Europe and the fragmentation of trading platforms, clearing systems and settlement systems in capital markets provided large practical hurdles to the coming together of exchanges from separate jurisdictions.

These impediments presented a challenge which could only be overcome in a specific regulatory climate. Fortunately, EU regulatory and policy changes in the late 1990s and early 2000s provided the optimal conditions for the convergence of securities exchanges.

B Regulatory Climate

In the period immediately preceding the Euronext merger, the EU pursued a rapid course of financial reform. With the launch of the Euro in 1999, integration of European financial sector and broader market was clearly on the agenda.²² This could only be confirmed by the adoption by the EU of the Financial Services Action Plan in 1999,²³ the Lamfalussy Report,²⁴ subsequent creation of pan-European oversight (but not regulatory) bodies and implementation of EU-wide directives. These initiatives, taken cumulatively went some way to facilitating, if not providing the basis for the convergence of the Euronext securities exchange. This section tracks the regulatory challenges and reform which emerged in the late 1990s and early 2000s.

In 1999, the EU was faced with some key impediments within its existing securities regulation. The largest problems were faced by issuers who wanted to make cross-border offerings. Firstly, there was a need to produce multiple sets of official documentation meeting different disclosure requirements of each member state in which an offer was to be made, second, the fragmentation of financial ongoing reporting regimes across Europe meant that different sets of ongoing disclosure information had to be produced by issuers in each member state that they issued shares, and third the different marketing rules for retail offers

²² Faruk Balli, Syed Abul Basher and Hatice Ozer-Balli, ‘From Home Bias to Euro Bias: Disentangling the Effects of Monetary Union on the European Financial Markets’ (2010) 62 *Journal of Economics and Business* 347, 347.

²³ NYSE Euronext, ‘Amendment No. 1’, above n 9, 50.

²⁴ Lamfalussy et al, above n 11.

in each member state meant that it was difficult for issuers to pursue a single course of action without considering multiple sets of marketing regulations.²⁵

In response to these problems, the EU released the FSAP, the first strategic objective of which was creating ‘a single EU wholesale market’, allowing corporate issuers to raise capital on a pan-European basis.²⁶ This objective showed that the EU was beginning to acknowledge the importance of capital markets to its future prosperity and the necessity for a pan-European approach to growth. Within this strategic objective, were enumerated 19 specific means by which it would be accomplished. From the issuer’s perspective, these measures were beneficial because they sought to ‘overcome obstacles to the effective mutual recognition of prospectuses, so that a prospectus or offer document approved in one Member state will be accepted in all’ member states, and to simplify the requirements with regard of regular reporting.²⁷ From the flailing European retail investor’s point of view, incentive would be given to invest to a greater extent in securities because the FSAP sought to provide access to all markets from a ‘single point of entry’, and to enhance market confidence by making publically available more information.²⁸

The EU sought to facilitate the goals set forth in its first strategic objective by the institution of its second objective – creating the conditions for ‘open and secure retail markets’.²⁹ This objective essentially went to unifying the expectations of member states with regard to the provision and marketing of financial services around Europe. This would go some way to allowing issuers and providers of financial services to conduct their business in accordance with a single set of rules.

The FSAP was ambitious, though much needed. More ambitious however, was the goal set at the Lisbon European Council in March 2000 of implementing the plan by 2005.³⁰ In 2001, the Lamfalussy report discussed some of the issues which would be encountered its implementation, as well as, importantly, suggesting the organisational structures that could realistically be created to bring its strategic objectives to life.³¹ Among the factors the Lamfalussy Committee listed as inhibiting both European financial growth and the

²⁵ Raj Panasar and Phillip Boeckman (eds), *European Securities Law* (Oxford University Press, 2010) 6.

²⁶ ‘Financial Services Action Plan’ (Communication of the European Commission, No 232, 11 May 1999) 22.

²⁷ Ibid.

²⁸ Ibid.

²⁹ Ibid 23.

³⁰ Panasar and Boeckman, above n 25, 5.

³¹ For a full summary of all of the foreseen issues with unification of the financial sector, see Richard K Abrams and Michael W Taylor, ‘Issues in the Unification of Financial Sector Supervision’ (Working Paper No WP/00/213, International Monetary Fund, 2000).

development of pan-European governance were the absence of Europe-wide regulation, inconsistent implementation of directives by EU member states and the large number of transaction and clearing and settlement systems that fragment liquidity and increase costs.³²

In response to these concerns, the Lamfalussy Committee suggested four tiers of European governance which would go some way to giving the regulatory oversight required to have a pan-European approach to securities regulation.³³ Within the third of these four tiers was to sit the European Securities Regulators Committee ('CESR'). CESR was originally conceived as a cooperative network of national regulators to promote consistent implementation of initiatives produced by the Lamfalussy process by developing guidelines and grouping of regulators. However, as time went on, CESR's technical expertise and market experience allowed it to take on an oversight role with respect to the national regulators. Its role grew to include peer review, mediation, best practice sharing and institutional support of cross-border cooperation concerning market abuse and the enforcement of financial reporting standards. In 2004, in accordance with the Lamfalussy recommendations, the EU created two other bodies, known as the alongside CESR, known as the Committee of European Banking Supervisors (CEBS) and the European Insurance and Occupational Pensions Authority (EIOPA). These bodies were known as the 3L3 (three level three) committees.³⁴ After the GFC, the 3L3 bodies came to be critiqued by the de Larosière Report, which noted that the committees were no longer equipped to deal with the 'number of inefficiencies' which had arisen in the recent past.³⁵ Primarily the two biggest issues with the 3L3 were that their recommendations could be ignored without repercussion and there was an absence of private rights available, which had become increasingly important in light of the recent crisis.

Substantively, the EU implemented a number of directives which provided an accommodating climate for the convergence of the Euronext market. By 2005 the following directives had been passed in accordance with the Lamfalussy Report:

- The Market Abuse Directive;³⁶

³² Lamfalussy et al, above n 11, 11.

³³ Noting that the Lamfalussy report stopped short of suggesting a pan-European regulatory framework because creating such a body would have involved amending the *Treaty of Rome*. Post-GFC however, the EU overcame this difficulty by using a delegation power from the European Commission under Article 290 of the *Treaty on the Functioning of the European Union* and created the European Securities and Markets Authority ('ESMA') which functions as a pan-European regulator.

³⁴ Council Directive 2004/5/EC of 20 January 2004 [2004] OJ L14/19.

³⁵ Jacques De Larosière et al, 'The High-Level Group on Financial Supervision in the EU' (Report, European Union, 25 February 2009) 46-47.

³⁶ Council Directive 2003/6/EC of 28 January 2003 on Insider Dealing and Market Manipulation (Market Abuse) [2003] OJ L 96/16.

- The Prospectus Directive;³⁷
- The Transparency Directive;³⁸
- The Takeover Directive;³⁹ and
- The Markets in Financial Instruments Directive.⁴⁰

These directives went some way to providing single European-wide standards to be met by issuers and regulatory agencies throughout Europe, and contributed therefore to the creation of an accommodating climate for an expanding European securities exchange such as Euronext.

C The Mandate Set Forth by Euronext Directors

In the context of rapid internationalisation, demutualisation, dematerialisation and regulatory development, the time was right for the Euronext exchanges to merge.

When the Amsterdam, Paris and Brussels stock exchanges agreed to come together in a merger, Jean-Francois Theodore, chief executive of the Paris Bourse explained that ‘this is what our members have been demanding, cross border trading and liquidity,’ adding that the ‘savings will be huge’ on cross-border trading with a common information technology and trading network.⁴¹

In his speech announcing the merger, Theodore said:

EURONEXT is not just another merger. It is the first attempt to take advantage of the immense potential of the European financial market opened by the implementation of the single currency. Compared to the US, the European financial market has still room for growth. And it is already undergoing significant changes, from savings to securities, from debt to equity, from domestic to cross border. On our stock markets, volumes are skyrocketing and all studies forecast this dramatic growth will continue in the coming years. Still, Europe's financial markets remain fragmented and domestic, with more than 30 different trading and clearing systems combined with different national regulations. Most European exchanges offer state of the art electronic trading and clearing systems and excellent listing services on national securities. But they still lack the pan-European dimension. For global intermediaries and issuers this situation is an expensive paradox. They would like to benefit

³⁷ Council Directive 2003/71/EC of 4 November 2003 on the Prospectus to be Published when Securities are offered to the Public or Admitted to Trading and Amending Directive 2001/34/EC [2003] OJ L 345/64.

³⁸ Council Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the Harmonisation of Transparency Requirements in Relation to Information About Issuers whose Securities are Admitted to Trading on a Regulated Market and Amending Directive 2001/34/EC [2004] OJ L 390/38.

³⁹ Council Directive 2004/25/EC of 21 April 2004 on Takeover Bids [2004] OJ L 142/12.

⁴⁰ Council Directive 2004/39/EC of 21 April 2004 on Markets in Financial Instruments Amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and Repealing Council Directive 93/22/EEC [2004] OJ L 145/1.

⁴¹ ‘European Bourses Merge’, *CNN Money* (online), 20 March 2000 <http://money.cnn.com/2000/03/20/europe/merger_exchanges/>.

from the additional liquidity, the reduced cost of capital, and the improved cross-border trading and clearing conditions integrated pan-European capital markets could bring.

EURONEXT addresses their needs. It is the first exchange to offer users a fully integrated trading, netting, clearing and settlement solution on a pan European basis. EURONEXT will have one single order book, one single rule book, one single trading system, one single counterparty, one platform for settlement. For these two last points, keep in mind that in January CLEARNET SA will unify the clearing structures of our three exchanges and that our three national CSDs will merge into EUROCLEAR. This will generate -beginning next year- huge economies of scale for intermediaries and investors alike.⁴²

The Euronext Annual Report of 2000 echoed these grand ambitions, stating:

[W]e did not create Euronext just so we could grow. We created Euronext in order to answer the growing demand from the market for further consolidation in the European capital market and a desire for greater liquidity at lower costs, which we will strive to provide.

Euronext was created so that when our planned integration has been completed, we will be able to provide a single list of issuers and one technical platform for each of cash trading and derivatives trading. In turn, we believe that this will allow us to offer our customers, intermediaries and investors, access to a larger pool of liquidity from three countries with already efficient capital markets and high rates of savings, a wider choice of companies ranging from blue chips to high-growth small caps and mature mid caps, and a larger selection of investment products, including equities, derivatives, warrants, certificates, commodities and new products such as trackers and the Euronext indices.

Euronext also wants to provide the best services at the lowest possible cost. The merger should bring significant benefits to both users and shareholders in the form of the unified markets we intend to create with enhanced liquidity, transparency and price formation. The extension of Clearnet, the state of the art central counterparty that facilitates the netting of trades, from Paris to all Euronext markets, should considerably reduce the amount of capital users need to finance their trading activities and streamline clearing and settlement to achieve cost efficiencies.⁴³

While these goals are rather abstract, some of the more concrete goals, as described by Ulf Neilsson included cutting costs to all market participants, attracting more foreign listings, offering a wider selection of investment products and deepening liquidity pools.⁴⁴

III THE ORGANISATION AND GOVERNANCE STRUCTURE OF EURONEXT NV

A Organisation

On September 22, 2000, the Amsterdam, Brussels and Paris exchanges came together in the first ever merger to create a cross-border stock exchange. This was one of the first examples of a set of exchanges reacting to an increasingly competitive market. This part explains the

⁴² Jean-François Théodore, Chairman and Chief Executive Office of Euronext, 'Birth of Euronext' (Speech delivered in Amsterdam on 22 September 2000) <http://www.paris-europlace.net/dossiers001_fr.htm>.

⁴³ Euronext, 'The Year 2000' (Company Report, 2000) < <https://corporate.nyx.com/investor-relations/euronext-nv-financials/ir-archives/annual-reports> > 5.

⁴⁴ Ulf Neilsson, 'Stock Exchange Merger and Liquidity: The Case of Euronext' (2009) 12 *Journal of Financial Markets* 229, 238.

mechanics of the merger, the structure of the composite exchanges and the resulting cross-border exchange, and how eventually, the Euronext market came to incorporate the Lisbon exchange and the LIFFE, and itself become a listed company.

Of the three constituent markets, the Amsterdam stock exchange was the first to demutualise in 1997 and therefore become capable of merger activity.⁴⁵ Both the SBF and the BSX became demutualised during the actual merger process.

For the purposes of facilitating the merger, Euronext NV, a company domiciled in the Netherlands, was created by the SBF, BXS and the AEX on July 20, 2000.⁴⁶ As described in the 2000 annual report of the newly founded company:

[T]he three constituent companies merged into Euronext N.V. As regards SBF and BXS, the merger was implemented by means of a transfer to Euronext N.V. of SBF-shares and BXS-shares held by the relevant shareholders in exchange for new Euronext N.V. shares. With respect to AEX, the merger was effected by means of a three-way legal merger between AEX, Euronext N.V. and its wholly-owned subsidiary Euronext Amsterdam N.V. In this merger, all assets and liabilities of AEX were transferred to Euronext Amsterdam N.V. and the shareholders and holders of profit-sharing certificates of AEX became shareholders of Euronext N.V. SBF and BXS were renamed Euronext Paris S.A. and Euronext Brussels S.A., respectively, after 22 September 2000.

Euronext N.V. operates stock and derivatives exchanges through subsidiaries in Paris, Brussels and Amsterdam. The range of services includes listing of financial instruments, the organisation of trading in such instruments, clearing, settlement, custody and the sale of related information and products.⁴⁷

Following the merger, 60% of Euronext NV shares became owned by former SBF shareholders, 32% became owned by former AEX shareholders and former holders of participating certificates issued by AEX, and 8% became owned by former BXS shareholders.⁴⁸

Initially, the merger was intended to involve only the integration of their clearing arrangements. However, the three exchanges soon realised that greater efficiencies could be obtained if they also integrated their trading functions. Eventually, all financial instruments would be traded on a single integrated trading platform, and that the listing and trading rules of the merged exchanges would be harmonized, resulting in a single market rulebook, with

⁴⁵ Pamela S Hughes, 'Background Information on Demutualization' in Shamshad Akhtar (ed), *Demutualization of Stock Exchanges: Problems, Solutions, and Case Studies* (Asian Development Bank, 2002) 33, 40.

⁴⁶ Euronext, 'The Year 2000', above n 43, 27.

⁴⁷ Ibid.

⁴⁸ Ruben Lee, 'Changing Market Structures, Demutualisation and the Future of Securities Trading' (Working Paper, 5th Annual Brookings/IMF/World Bank Financial Markets and Development Conference, 15 April 2003) 11.

issuers subject to the supervision and monitoring rules, information obligations and public offer obligations set by the regulators in the country in which they are listed.⁴⁹

However, this endpoint was easier envisaged than executed. The trading platforms in Brussels and Paris were relatively similar, but differed significantly from the platform used in Amsterdam. While in Brussels and Paris cash trading took place through an electronic public limit-order book where orders were matched together, the Amsterdam cash market relied on the ‘Hoekman’, whose role was similar to that of the specialist found on the New York Stock Exchange.⁵⁰ As is described in the below ‘Trading Platforms’ section, the integration gradually took place over three stages, firstly through integration of cash trading platforms, then of derivatives trading platforms and lastly of clearing platforms.

At the time Euronext NV merged, the governance structure was described in the Euronext 2000 company report as follows:

In accordance with Dutch law, Euronext has a two-tier board structure. The management of Euronext N.V. by the Managing Board and the supervision by the Supervisory Board are separate and different responsibilities.

The Managing Board is under the direction of the Chairman (also Chief Executive Officer). Besides the CEO, the Managing Board also comprises the Chief Operating Officer and the Executive Vice-President. The Managing Board as a whole is responsible for the management of the company. The Managing Board has adopted an internal allocation of duties for each of its members, including the specific duties and powers of the CEO. The allocation of duties requires the approval of the Supervisory Board. The internal allocation of duties also contains provisions regarding the titles as used within the Managing Board and the details of the way the chairmanship of the Managing Board rotates. The CEO, Mr Théodore, will be the Chairman of the Managing Board for a period of four years starting in 2000. After this period, a person with Dutch nationality will act as Chairman for the same length of time. The members of the Managing Board are appointed by the Supervisory Board, which also determines the number of members. Members of the Managing Board may be suspended or dismissed at any time by the Supervisory Board.

The Supervisory Board is in charge of the supervision of the Managing Board and the general course of affairs at the company and the business affiliated with it. Besides its formal tasks, the Supervisory Board assists the Managing Board by providing advice. The members of the Supervisory Board have to be independent from the company, and when performing their tasks must act in the interests of the company and the business affiliated with it.

Mr Hessels has been appointed Chairman of the Supervisory Board for a term of four years. He will be succeeded by a person with French nationality, who will also serve for a period of four years.

The financial statements are prepared by the Managing Board and have to be adopted by the Supervisory Board and then be approved by the Annual General Meeting. According to

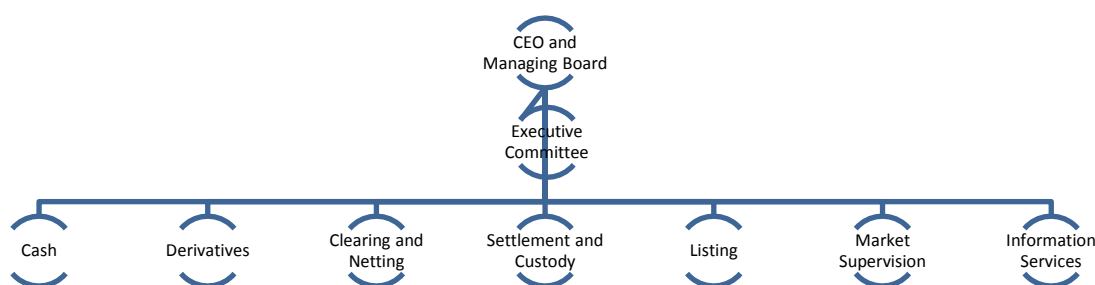
⁴⁹ Marco Pagano and A Jorge Padilla, ‘Gains from Stock Exchange Integration: The Euronext Evidence’ (Centre for Economic Policy Research, May 2005) <<http://www.ilsole24ore.com/art/SoleOnLine4/Finanza%20e%20Mercati/2006/05/padilla-pagano.pdf>> 10.

⁵⁰ Ibid.

Euronext's articles of association, important decisions require the approval of the Supervisory Board. The different responsibilities of both the Managing Board and the Supervisory Board are laid down in an authorisation schedule, which has been approved by the Supervisory Board.

Members of the Supervisory Board will be appointed by the Supervisory Board. The appointment of members of the Supervisory Board has to be in line with a pre-agreed profile of the composition of the Supervisory Board. The Supervisory Board's current composition is based on a preliminary profile, and a final profile will be adopted in 2001. Members of the Supervisory Board resign after four years have passed since their last appointment and may be reappointed. A rotation schedule was adopted by the Supervisory Board that enables a proper resignation roster. The Annual General Meeting, the works council and the Managing Board have the authority to nominate candidates for appointment as members of the Supervisory Board. The Annual General Meeting of shareholders and the works council also have the authority to raise objections against the appointment of a candidate as a member of the Supervisory Board.⁵¹

The Euronext corporate governance structure, immediately post-merger, is here depicted:



After establishing itself in 2000, Euronext pursued an aggressive growth strategy, which began by making an IPO of its own shares. On July 5, 2001, Euronext NV made a public offering of 24.86% of its shares.⁵² Euronext shares were originally listed on the Premier Marché, SBF 120 index, in Paris in November 2001 and then on the Next 150 index in January 2002.⁵³ Shares were originally priced at €24 and were mostly sold to institutional investors, through a retail offering was made in France, Belgium and Netherlands and was oversubscribed, and the share price sharply rose.⁵⁴ The total market capitalisation of this offering was EUR 693 million, comprising 16.7 million new shares and 12.2 million existing shares.⁵⁵

⁵¹ Euronext, 'The Year 2000', above n 43, 64.

⁵² Euronext, 'Annual Report 2001', above n 2, 45.

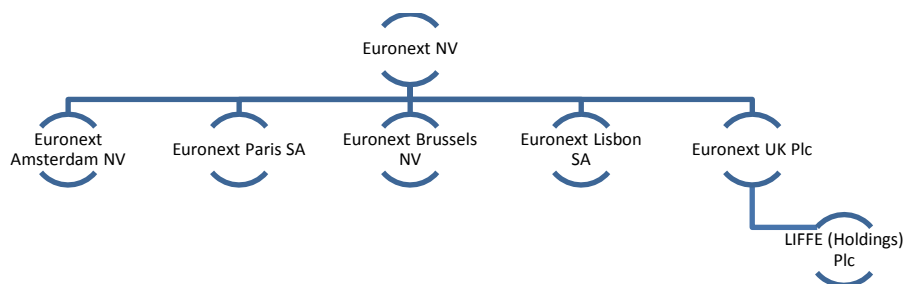
⁵³ Ibid.

⁵⁴ Leighton-Jones and Jeffs, above n 5; 'Euronext IPO Successfully Completed – IPO Price: EUR 24 per Share', *Mondo Visione* (online), 5 July 2001 <<http://www.mondovisione.com/news/euronext-ipo-successfully-completed-ipo-price-eur-24-per-share/>>.

⁵⁵ 'Euronext IPO Successfully Completed – IPO Price: EUR 24 per Share', above n 54.

The next major growth landmarks for Euronext NV were its acquisition of the LIFFE and merger with the BVLP. On October 2, 2001, the LIFFE board unanimously opted to accept an offer from Euronext NV, to acquire the futures exchange for a price of £555m, or £18.25 per share.⁵⁶ This acquisition followed a hard fought bidding battle with the London Stock Exchange. Thereafter in February 2002, the shareholders of the BVLP unanimously accepted a merger offer from Euronext NV and the BVLP became Euronext Lisbon, a wholly owned subsidiary of Euronext NV. Euronext issued 4.8 million new shares and paid EUR 35 million in cash in exchange for the six million BVLP shares received from BVLP original shareholders.⁵⁷

The following diagram illustrates the company structure after all of the above merger activity:⁵⁸



B Rules

One of the fundamental goals of the Euronext exchange was pan-European operation according to a single set of rules. Clearly, the rapid consolidation of multiple exchanges, all operating according to the regulations of different national regulators is not a system which is particularly amenable one single set of rules. It is for this reason that the later NYSE-Euronext exchange continued to operate according to two sets of rules. On the one hand, there are a set of ‘harmonised rules’, according to which all of the Euronext exchanges operate, which cover membership, market access arrangements, securities and derivatives trading rules, listing and conduct rules and punitive measure in response to violations.⁵⁹ On the other hand there are non-harmonised rules, which are specific to each of the constituent Euronext exchanges. These govern areas which vary between jurisdictions, in particular,

⁵⁶ ‘Liffe Chiefs Back Euronext Bid’, above n 3.

⁵⁷ ‘BVLP Joins Euronext’, above n 4.

⁵⁸ Noting that the intricacies of all of the clearing systems and subsidiaries of the national exchanges have been omitted, they can be seen here: Euronext, ‘Annual Report 2002’ (Company Report, 2002) <http://www.zonebourse.com/EURONEXT-16725768/pdf/8369/EURONEXT_Rapport-annuel.pdf> 24-25.

⁵⁹ See, eg, Euronext, *Euronext Rule Book—Book I: Harmonised Rules*, 9 March 2015 <<https://www.euronext.com/en/regulation/harmonised-rules>>.

things like financial instruments which may be placed on the exchange, public offering rules and rules applicable to listing and delisting financial instruments.⁶⁰

C Regulation of Euronext

Between 2000 and 2007, and until 2010 the national regulators of the Euronext exchanges were parties to two Memoranda of Understanding ('MOU') that provided a framework for the coordination of their supervision of Euronext NV and of the markets operated by the Euronext group.⁶¹

The first MOU was initially entered into by the Dutch, French and Belgian exchange regulatory authorities in 2001 and was extended to the Portuguese exchange regulatory authority in 2002.⁶² The second MOU, which relates principally to the regulation of Euronext's derivatives markets, was entered into between such authorities and the UK exchange regulatory authority in 2003.⁶³

The principal forum for coordinated supervision under the MOUs is was the Chairmen's Committee, which was composed of the chairmen of each of the signatory regulatory authorities. The Chairmen's Committee took decisions by consensus and met regularly with Euronext's managing board. Before meetings of the Chairmen's Committee, a Steering Committee consisting of representatives of the member regulators, which could create working groups on certain issues to be brought before the Chairmen's committee. Following a decision by the Chairmen's and Steering Committees, the members of the committee which acted were required to recommend to their home regulatory authority to approve, adopt and otherwise act in accordance with the decision.⁶⁴

Decisions requiring prior approval of the Chairmen's Committee included entering into alliances, mergers, cross shareholdings and cross-membership agreements, performing certain integration and restructuring steps, listing of shares of Euronext or its subsidiaries,

⁶⁰ Euronext, *Euronext Rule Book—Book II: Specific Rules Applicable to the French Regulated Markets*, 6 October 2014 <<https://www.euronext.com/en/regulation/paris>>.

⁶¹ NYSE Euronext, 'Amendment No. 1', above n 9, 50.

⁶² *Memorandum of Understanding Between The Authority for the Financial Markets (The Netherlands), The Autorité des Marchés Financiers (France), The Banking Finance and Insurance Commission (Belgium) and The Comissão do Mercado de Valores Mobiliários (Portugal) on the Coordination, Supervision and Oversight of the Euronext Group*, signed 22 March 2001.

⁶³ *Memorandum of Understanding Between The Commission Bancaire et Financière (Belgium), Conseil des Marchés Financiers (France), Commissin des Opérations de Bourse (France), Netherlands Authority for the Financial Markets (The Netherlands), Comissão do Mercado de Valores Mobiliários (Portugal) and The Financial Services Authority (UK) Regarding the Coordinated Regulation and Supervision of the Derivatives Markets Operated by the Euronext Group and of Euronext NV*, signed 6 March 2003.

⁶⁴ NYSE Euronext, 'Amendment No. 1', above n 9, 51.

outsourcing activities related to trading, registration and publication of transactions, surveillance of trading members' activity monitoring of transactions, creating or closing a regulated market or other trading facilities and approving or modifying the bylaws of Euronext NV or its subsidiaries. In addition, it was necessary for the Chairmen's Committee to approve any modifications to the Euronext Rulebook. Decisions subject to the non-opposition of the Chairmen's Committee include issuing notices interpreting or implementing provisions of the Euronext Rulebook and appointing (i) members of Euronext's managing board and supervisory board and (ii) key personnel. Decisions requiring notification to the Steering Committee include the admission, sanction, suspension or exclusion of a market member, and certain other decisions such as listing or delisting of a financial instrument, suspension of trading, or other events that may be agreed between the signatory authorities.⁶⁵

Matters not specifically delineated by the MOUs were reserved to the national regulators.

D National Regulation

Each of the Euronext list exchanges contained stock exchanges, derivatives markets or both, holding licences in their home jurisdictions to operate regulated markets:

- Euronext Amsterdam operated one stock market (Eurolist) and one derivatives market (Euronext Amsterdam Derivatives Market)
- Euronext Brussels operated two stock markets (Eurolist and the Trading Facility) and one derivatives market
- Euronext Lisbon operated one stock market (Eurolist) and one derivative market (Portugese Futures and Options Market)
- Euronext Paris operated one stock market (Eurolist) and two derivatives markets (MONEP and MATIF)
- LIFFE operated one derivative market (London International Financial Futures and Options Exchange)

Each market operator was subject to national laws and regulations. The regulatory authorities that were signatories to the MOUs agreed to use their best efforts to harmonize their respective national rules, regulations and supervisory practices regarding listing requirements, prospectus disclosure requirements, ongoing obligations of listed companies, take-over bid rules and disclosure of large share holdings. The rules regarding public

⁶⁵ Ibid.

offerings of financial instruments and prospectuses as well as ongoing (ad-hoc and periodic) disclosure requirements for listed companies were set forth by the Prospectus Directive and Transparency Directive which must be implemented in Euronext countries by each legislative body and regulator. In order for companies seeking to list and trade their securities on a Euronext market it was necessary to comply with the harmonized listing requirements of Rulebook I and, following admission, with the ongoing disclosure requirements applicable in the country in which the relevant market is located.⁶⁶

Companies could apply for admission to listing and trading in one or more jurisdictions in which a Euronext market was located. However, as is explained in the next section, a single point of entry for issuers allows investors from other Euronext countries to have access to the order book in all markets as far as trading is concerned.

E Trading Platforms

By 2005, before Euronext merged with the New York Stock Exchange, it had created harmonised IT platforms for cash trading and listing, called the Nouveau Système de Cotation ('NSC'), and for derivatives, called LIFFE CONNECT.⁶⁷ In cash and derivatives markets, these systems allowed market participants, both at the issuer and investor ends of the transaction, to access all Euronext markets, not their original entry point market. For cash markets, a single list was created, called Eurolist, and for derivative markets all equity option contract sizes were harmonised.⁶⁸ Furthermore, a single trading fee structure had been implemented across both the cash and derivatives markets.

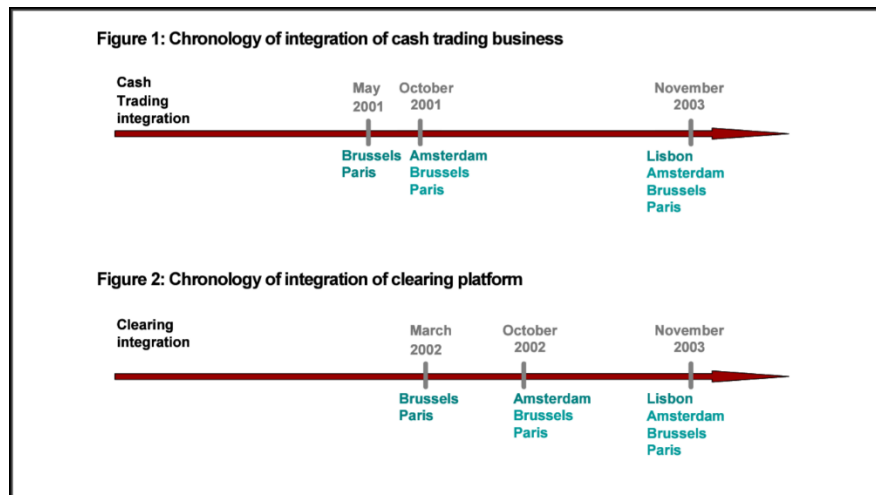
The integration process was not as simple as the resulting single integrated market product makes it seem. As mentioned above, with respect to cash trading, the Amsterdam cash trading system, which was used on a specialist model, was quite different to the Brussels and Paris exchanges, which used a limit-order book. The integration process was also greatly affected by the above mentioned integration of the BVLP and LIFFE markets. Padilla and Pagano provide a useful chronology in their 2005 analysis of the Euronext merger.⁶⁹

⁶⁶ Ibid 52.

⁶⁷ Euronext, 'Registration Document and Annual Report 2005' (Company Report, 2005) <http://www.zonebourse.com/EURONEXT-16725768/pdf/44549/EURONEXT_Rapport-annuel.pdf> 12, 18.

⁶⁸ Ibid 16.

⁶⁹ Pagano and Padilla, above n 49, 12.

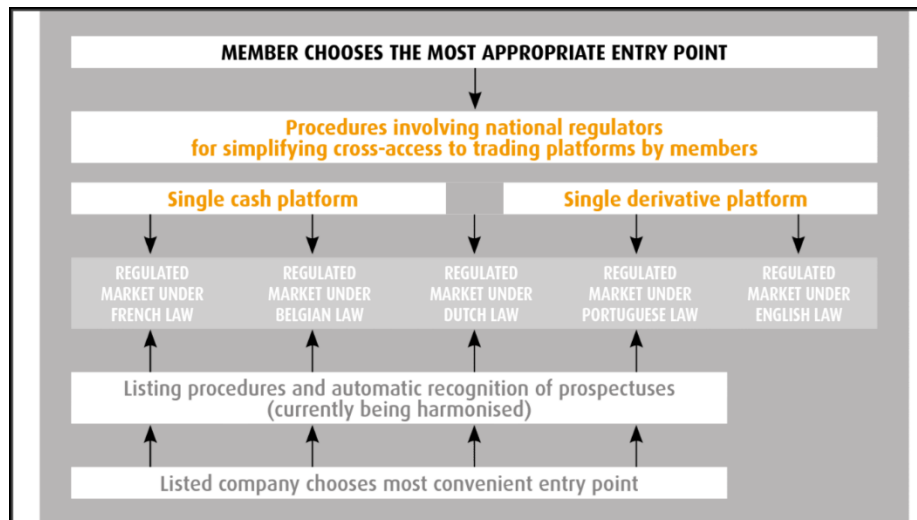


By 2004, companies applying for admission to listing on a Euronext exchange followed the same listing rules regardless of the point of entry to the market they chose (Amsterdam, Brussels, Lisbon or Paris). Once admitted by the relevant regulatory authorities, the company was then included in the appropriate Euronext segment, and selected a method of trading appropriate to the level of liquidity in its shares. After the listing is made, the securities were traded on a single market between all of the constituent exchanges.

On the other side of the transaction was the investor. In order to purchase and trade securities, the member chose the appropriate market and complied with the Euronext rules and securities regulation of that jurisdiction. The member then had access to the single trading platform and therefore the securities listed on each of the Euronext markets.

The following diagram was provided in Euronext NV's 2005 Annual Report to explain this process:⁷⁰

⁷⁰ Euronext, 'Annual Report 2005', above n 67, 19.



This is a system of mutual recognition between regulators, and as such significantly reduced the cost of trading for issuers, intermediaries and investors.

IV THE REACTION OF CONSTITUENT MARKETS TO THE EURONEXT MERGER

With the benefit of hindsight, several observers have been able to gauge the impacts of the Euronext merger on the constituent markets of Euronext according to economic and regulatory indicators. This literature has brought to light both benefits and drawbacks associated with the merger. This section talks through some empirical studies and literature on the merger.

A Benefits

1 Increase in Market Efficiency

In 2012, Khan and Vieito analysed the merger of Euronext NV with the BVLP, specifically with respect to the informational market efficiency of the market pre and post integration.⁷¹ A market is considered efficient if the price of an asset is an unbiased estimate of the true value of the asset. In an efficient market, prices are not necessarily always equal to the true value, though errors in market prices must be unbiased, meaning random. If the deviations from the true value are random, the probability that at any given time, that the price will be higher or lower than the true value of the asset will be equal, and there will be no correlation of price variations.⁷² The strength of market efficiency depends an assumption about the information

⁷¹ Walayet Khan and Joao Paulo Vieito, 'Stock Exchange Mergers and Weak Form of Market Efficiency: The Case of Euronext Lisbon' (2012) 22 *International Review of Economics and Finance* 173.

⁷² Ibid 174.

taken into account when asset prices are determined. Weak market efficiency assumes that the actual price of an asset incorporates only data about past prices of assets. Semi-strong market efficiency assumes that all publicly available information is incorporated into the price of an asset and strong market efficiency assume that all information, public and private is incorporated in the prices of assets. Khan and Vieto's study was only on *weak* market efficiency.

They found that according to some tests market efficiency improved, and according to others, market efficiency 'either improved or stayed the same'. This showed them that, although the findings of some tests were mixed, there was a tendency of improved efficiency for a large number of companies.⁷³

2 Decreased Costs of Trading

In 2005, Padilla and Pagano conducted an extensive study on the effect of the Euronext merger for the costs of trading for investors in the constituent markets. They analysed both the 'explicit costs' of trading, such as exchange fee, commissions, and the costs of clearing and settlement, and 'implicit costs', which include the bid-ask spread and the price impact of orders, to the extent that large orders cause an adverse change in security process. Padilla and Pagano noted that:

Integration can reduce the explicit costs of trading for at least three different reasons:

- Integrating the operations of the exchanges can eliminate duplication of their fixed costs and thereby reduce the average cost of a trade for the exchange. There is evidence that these economies of scale can be substantial. Competitive constraints from other trading platforms and from users will induce the exchange to pass on these cost reductions to the members of the exchange in the form of reduced exchange fees.
- These efficiency gains extend to the post-trading phase as well: stock market integration results in a larger volume of trading activity (see below) which increases the efficiency of the clearing and settlement mechanism; in particular, by allowing the netting of a larger volume of trades.⁴ Again, these reductions in costs can be passed through to users in the form of lower fees charged by the relevant platform.
- Accessing a single trading platform instead of two (or more) allows market professionals to save on the hardware, software and skilled human capital necessary to access and monitor separate trading platforms. These savings can be passed-on to final investors in the form of reduced commissions

Stock market integration can also reduce the implicit costs of trading:

- First, by fostering trading activity, it tends to reduce bid-ask spreads insofar as it:
 - helps intermediaries to defray fixed order processing costs—namely, the costs of access to the trading platform and of maintaining a continuous market presence;

⁷³ Ibid 188.

- reduces adverse-selection costs, due to the presence of informed traders, provided that the additional order flow comes mainly from uninformed traders or elicits more aggressive competition between informed ones;
 - reduces the inventory-holding costs of market makers, as it makes the order flow more predictable and lowers the costs of rebalancing market-makers' inventories after the execution of large orders; and
 - induces entry by market professionals (brokers and market-makers), and thereby leads to greater competitive pressure both in quote-setting and in brokerage fees.
- Second, the increase in liquidity can reduce the price concession an investor has to accept to execute a relatively large order. Greater liquidity may be associated also with lower price volatility, insofar as a larger and more stable order flow reduces the noise induced by individual orders, and a lower bid-ask spread lowers the "bid-ask bounce" of transaction prices.⁷⁴

Padillo and Pagano found that the explicit costs of the Euronext market were reduced in the areas of IT consolidation, including cash trading, derivatives and clearing, as well as significantly reduced staff costs, created by centralising operations. They also found that the implicit costs were reduced for user of the market, generated largely by the rise in market liquidity (discussed below) generated by the merger.⁷⁵

They also looked at the direct benefits to users of the market. Specifically, they noted that there was more efficient and cheaper access to Euronext markets due to wider trading opportunities, an increase in direct, non-intermediated trading and an increase in cross-border trading, decreased transaction costs for investors, brokers and intermediaries, simpler access to markets, and increased market liquidity.⁷⁶

3 Increase in Liquidity of Markets

In one of the most comprehensive empirical analyses of the Euronext NV mergers, Ulf Neilsson investigated the effects of the mergers on listed firms of the former SBF, BSX and AEX exchanges. In particular, he analysed how exchange consolidation affected stock liquidity, and what types of firms benefit the most in terms of stock liquidity.⁷⁷

As Neilsson explains, the main motivation for studying liquidity is that it ultimately affects the cost of capital. If the trading volume of a stock is low, it is harder to sell and the bid-ask spread is high. The analysis showed that, while there were significant liquidity gains for large

⁷⁴ Pagano and Padilla, above n 49, 7.

⁷⁵ Ibid 50.

⁷⁶ Ibid 28-32.

⁷⁷ Neilsson, above n 44.

firms post-merger, the same effect was not observable in small and mid-sized firms. It should be noted however that there was nothing to suggest a decrease in liquidity in smaller firms. This is supported by the above research conducted by Padilla and Pagano.⁷⁸

These results may be attributable to home bias (discussed below), which could mean that investors seek only to purchase the securities of non-local companies if they are large, recognisable firms.

Nonetheless, increased liquidity is a good indicator of overall success of the merger.⁷⁹

4 Raised Standard of Financial Reporting

In 2012, Pownall, Vulcheva and Wang conducted a study on the effect of the Euronext merger on the reporting and disclosure of firms on the Euronext market. As a preliminary point, they describe a phenomenon known as ‘bonding’, which describes the process where firms trading on a cross-border exchange ‘bond’ to higher standards of financial reporting quality and transparency.

They note that often consolidated markets fail to create deeper pools of liquidity if monitoring and enforcement of securities regulation is dissimilar. Trading on consolidated markets may be hindered when firms from the legacy markets have to adhere to different reporting standards and securities regulation.⁸⁰

The Euronext market attempted to ensure consistency of market regulation of its constituent markets through the two above mentioned MOUs. According to the MOUs, the markets adhered to Rulebook I, with harmonised rules according to which all of the Euronext firms operate. This is said to have incentivised higher accounting standards by firms, whose transaction costs would have been reduced by complying with Euronext rules. Overall the study found that both accounting standards and liquidity increased post-merger.⁸¹

B Drawbacks

1 Herding

⁷⁸ Pagano and Padilla, above n 49, 46.

⁷⁹ Grace Pownall, Maria Vulcheva and Xue Wang, ‘Increasing Liquidity on Global Stock Exchanges: The Structure of Euronext’ (2015) *Accounting Horizons* [forthcoming] 1.

⁸⁰ Ibid 5.

⁸¹ Ibid 37.

Herding refers to individuals choosing to mimic the behaviour of others, following observation of each other's actions and pay-offs. Depending on the motive underlying imitation, herding can be intentional, or unintentional. Intentional herding is reflected in correlated actions motivated through the anticipation of payoffs in settings characterised by actual or perceived asymmetry. In the extreme, if the tendency of investors to follow others instead of focusing on private signals becomes widespread, 'cascades' are formed, which leads to the public pool of information to grow poorer. Reasons for herding may be career driven, with fund managers, who are assessed against their peers, copying other fund manager, or, in the case of unintentional herding, may be the result of a common background among traders.⁸²

Economou et al found that there was 'significant' herding in all four of the Euronext markets. This is attributed to the group's sophisticated structures, which facilitate the observation (due to the transparency of the exchanges) and imitation (possible because of the high liquidity of the market) of the action informed investors by their 'uninformed counterparts'.⁸³

2 *Eurobias*

Home bias refers to the phenomenon that investors everywhere tend to overinvest in domestic securities and underinvest in foreign securities relative to optimal global portfolio diversification, and has been observed in many contexts and time periods.⁸⁴

Balli et al note that, as a result of European market convergence and its surrounding factors, home bias has decreased in the European domestic markets, although it has been replaced with a 'Eurobias' where, instead of preferring their domestic securities, the investor prefers to purchase mainly European securities.⁸⁵

3 *Continued Fragmentation of Enforcement*

There is continuing criticism of the Euronext market, that, as a cross-border institution, it is unable to legitimately enforce its listing and disclosure requirements. Pownall, Vulcheva and

⁸² Fortini Economou et al, 'Herding Dynamics in Exchange Groups: Evidence from Euronext' (2015) 34 *Journal of International Financial Markets, Institutions & Money* 228, 229.

⁸³ Ibid 235.

⁸⁴ Grace Pownall, Maria Vulcheva and Xue Wang, 'The Ability of Global Stock Exchange Mechanisms to Mitigate Home Bias: Evidence from Euronext' (2014) 60 *Management Science* 1655.

⁸⁵ Balli, Basher and Ozer-Balli, above n 22, 349.

Wang point out that Euronext has no power of enforcement other than the threat of delisting, which is an unattractive option when the goal of the cross-border exchange is to maximise utility through garnering liquidity.⁸⁶ However, this may only have been indicative of a developmental period; traditionally exchanges as self-regulatory organisations, prior to the age of highly developed financial regulation, could only rely on custom, peer pressure and exclusionary tactics. Therefore, each of the constituent exchanges are regulated by their home regulators, the strength of which varies from jurisdiction to jurisdiction.⁸⁷ This latter criticism may now have dissipated in the face of the creation in 2011 of the pan-European regulator, the European Securities and Markets Authority. Euronext continues to this day, albeit after a tumultuous period between 2007 and 2014.

V CONCLUDING REMARKS

Overall, there are a few important things to note about the process leading to the consolidated Euronext market. Firstly, the founders of the exchange took advantage of the favourable economic and political decisions being made by the European Union in the period immediately preceding the 2000 merger. During this time, the EU demonstrated a wide spread political will to create an integrated financial system. The FSAP set forth in 1999 provided the grounding and confidence for the constituent exchanges to pursue their goal of consolidation, and the string of Directives passed in 2003 and 2004 provided the framework for them to do so.

In this favourable economic and political context, the Euronext exchange took advantage of the EUs consensus-based decision making and political goodwill to create a single trading platform for European securities. The merger parties sought to harmonise national regulation of participating markets by signing and acceding to MOUs.

Secondly, there were both benefits and drawbacks involved in the consolidation of the Euronext exchange. However, with greater liquidity and decreased operating costs, the Euronext market was more able to compete in the increasingly internationally-focussed global market. This was especially important for the Euronext Exchange as London and Frankfurt, two of the most prominent forces in the region, engaged in a merger in 2000,

⁸⁶ Pownall, Vulcheva and Wang, 'Increasing Liquidity', above n 79, 13.

⁸⁷ Norman S Poser, 'The Stock Exchanges of the United States and Europe: Automation, Globalization, and Consolidation' (2001) 22 *University of Pennsylvania Journal of International Economic Law* 497, 538. See also Howell E Jackson and Mark J Roe 'Public and Private Enforcement of Securities Laws: Resource-Based Evidence' (2009) 93 *Journal of Financial Economics* 207.

which created increased regional competition. As is discussed in the following chapter, the Euronext subsequently moved to fortify its position in the European region and the global market, by engaging in another merger with the New York Stock Exchange. In doing so, it solidified itself as one of the new breed of global securities exchanges which have emerged in the contemporary era.

A.2 BIG DEAL – NYSE EURONEXT*

I THE BIG DEAL – AND WHY IT HAPPENED

It was the big deal: the merger of the NYSE with Euronext, creating the first transatlantic exchange, and beating rival NASDAQ to the punch. The merger itch arose from ‘the spread of electronic trading, deregulation, demutualisation, and, last but not least, increased competition’.¹ At the time, a number of benefits, justifying the audacious move, were cited: cost savings, a bigger trading pool and increased liquidity, synergies among staff and stronger branding. Commentators painted a rosy picture.

An optimistic account of exchange consolidation states that integration promises synergies and scale benefits. IT is, for example, a major fixed cost for exchanges. Operation synergies can be achieved by eliminating redundancies associated with the development and operation of several IT systems. Streamlining or harmonizing technology can also be expected to reduce access costs for users which have to maintain connections with different trading systems. Consolidation should further allow the building of a larger liquidity pool by bringing the liquidity exchanges benefit from economies of scale, exchange integration should reduce trading costs. As a result new participants should enter the market which in turn should have a positive impact on trading volumes and liquidity. Finally, consolidation should hold benefits in terms of staff synergies, branding, improved visibility for companies listed on-exchange and product diversification. It is no secret that NYSE was eyeing Euronext.Liffe – the London derivative exchange – and that product diversification was an important impetus for the NYSE Euronext deal.²

Alliances were not a new phenomenon, but mergers provided more credibility, indicating a higher level of commitment.³ Accountability to shareholders would increase and a single board and chief executive would facilitate decision-making.

Electronic trading was transforming their business model and stronger exchanges were no longer simply absorbing weaker ones.⁴ Exchanges wanted to increase trading capacity and order flow in order to generate increased profits. With electronic trading, the costs associated with introducing new products on traditional floor-based exchange fell dramatically.⁵ Costly real estate became irrelevant.

* The author would like to acknowledge, in particular, the assistance of Nathan Qun Wai Ma with this chapter.

¹ Pierre Schammo, *Regulating Transatlantic Stock Exchanges* (2008) 57 *International and Comparative Law Quarterly* 827, 832 n 19.

² Ibid 832.

³ Ibid 832 n19.

⁴ Michael Gorham and Nidhi Singh, *Electronic Exchanges: The Global Transformation from Pits to Bits* (Elsevier Financial Markets Press, 1st ed, 2009) 166-168.

⁵ Ibid.

To be profitable, electronic exchanges must lower their average costs per contract,⁶ by increased trading in their existing contracts and adding product lines.⁷ Exchange consolidation results in more products trading on the same technology platform, reducing infrastructure costs.⁸ Lower average trading costs, leading to pumped up profits, became the driving force behind ‘a frantic quest to merge with other exchanges’.⁹

Competitive pressures, particularly with respect to the cost of technology upgrades, favoured larger entities.¹⁰ Mergers also had the effect of reducing competitive pressures on pricing of services.

II NYSE Euronext

A Demutualisation

The waves of demutualisation which facilitated exchange mergers began in Northern Europe with the Stockholm Stock Exchange.¹¹ Exchanges could list themselves, on themselves or other exchanges.¹² Stock exchanges were taking their cue from a similar trend in the insurance business.¹³

Why are they doing this now? The main motivation seems to be to provide a competitive advantage during a period of industry consolidation. If you want to acquire a competitor or even a financial company in a different line of business, using stock is often better than cash, especially when the stock market is overpriced. When buying an overpriced company, it's much better to pay it with your own overpriced stock than to use scarce cash. In addition, the owners of the acquired company are able to retain an interest in the new combination and to avoid the taxes associated with a cash sale. As both insurance companies and exchanges saw the mergers and acquisitions begin to take place, they knew that to compete in this game they needed a war chest full of their own stock – the ideal currency for acquisition.¹⁴

In old-fashioned mutual associations, decisions were made by members, and only members could trade.¹⁵ Demutualisation dissociated decision making from trading privileges.

B NYSE's transformation

⁶ Ibid.

⁷ Ibid.

⁸ Ibid 306.

⁹ Ibid 166-168.

¹⁰ Francis A Lees, *Financial Exchanges: A Comparative Approach* (Routledge, 1st ed, 2012) 269.

¹¹ Gorham and Singh, above n 4, 104

¹² Ibid 106, the Australian Securities Exchange is the first exchange in the world to list itself on its own exchange.

¹³ Ibid 107.

¹⁴ Ibid.

¹⁵ Ibid 108-109.

The New York Stock Exchange had long been the premier exchange in the US equities market.¹⁶ It demutualised and was publicly listed in 2006,¹⁷ ending 213 years of member ownership. The iconic trading floor had been ‘a highly visible symbol of the strength and vibrancy of the U.S. capital markets, making it a popular destination for foreign heads of state, corporate chiefs and A-list celebrities who seek the honor of ringing the NYSE’s opening and closing bell’.¹⁸

NYSE gained public company status through acquisition.

On March 7, 2006, the NYSE merged with publicly traded Archipelago Holdings Inc. to form the NYSE Group, shares of which began trading publicly the next day. Archipelago or Arca was an early electronic trading platform and had been a publicly traded company since August 2004. Arca had itself acquired a regional stock exchange, the Pacific Exchange in 2005. The New York Stock Exchange LLC was a wholly owned subsidiary under the holding company, NYSE Group Inc, which included the newly merged Archipelago Holdings.¹⁹

With Arca, the NYSE was able to execute trades electronically for the first time in its history.²⁰

Many motivations have been attributed to mergers between exchanges. The merger of NYSE with ArcaEx was based on the need to implement electronic trading quickly, constituting a dramatic revision of the business model. Also, that merger produced a more diversified revenue mix, including options trading. Finally, NYSE’s competitive position was vastly improved.²¹

In addition to acquiring electronic trading capacity in equities and options, with Archipelago the NYSE also became a leading provider of market data in these sectors.²² Driven by institutional investor demand for fast, efficient and anonymous computerised trading, electronic trading became a factor in the NYSE’s success in the ensuing years.

Personalities matter in exchanges, and the NYSE’s transformation began with the appointment of John Thain as CEO in December 2004.²³ Thain methodically introduced a modern trading platform,²⁴ recognising that radical change in a centuries old institution had to proceed incrementally. The result was a hybrid system; floor trading by specialists coexisted

¹⁶ ‘Factbox-Key Facts on NYSE-Euronext Merger’, *Reuters News* (online), 2 June 2006. <<https://global.factiva.com/>>.

¹⁷ Gorham and Singh, above n 4, 105, Table 5.1 of the chapter sets out a chronology of demutualization and IPO of financial exchanges.

¹⁸ Eric J Pan, ‘A European Solution to the Regulation of Cross-Border Markets’, (2007) 2 *Brooklyn Journal of Corporate, Financial & Commercial Law* 133, 134 n 4.

¹⁹ Gorham and Singh, above n 4, 119, a description on the process of NYSE becoming a public company.

²⁰ Pan, above n 18, 133.

²¹ Lees, above n 10, 106.

²² *Ibid* 91.

²³ *Ibid* 102-103.

²⁴ *Ibid*.

with electronic trading, satisfying proponents of both.²⁵ The NYSE could meet the diverse needs of customers – the electronic trading platform offering speed, certainty and anonymity and the traditional trading floor allowing for negotiation and price improvement to take place in the auction market.²⁶

C Why was NYSE Interested in Merging with Euronext?

1 Competitive Pressures of Globalisation

Cheap, improved communications had eliminated the need for multiple exchanges in most jurisdictions.²⁷ Competition among the survivors had been fierce, exerting downward pressure on settlement and clearance charges.²⁸ Regulators, too, had felt the pressures ‘to grapple with global and increasingly competitive financial markets and demands for greater and cheaper cross-border access by exchanges and financial market actors’.²⁹

In the race to attract cross-border listings, the advent of fully electronic trading put tremendous pressure on the NYSE;³⁰ it had to develop faster and more efficient systems. NASDAQ had led the charge as an operator of an advanced electronic trading platform as early as 2005. Other regional exchanges, like Philadelphia, Boston and Chicago, had abandoned the traditional trading floor in a move to fully electronic trading.

Electronic trading platforms facilitated off-exchange trading, breaking the trading monopoly of the traditional exchange.³¹

Traders in US-listed shares may deal directly with one another, or indirectly through ‘over the counter’ brokers, or new intermediaries. More than half of trading in Britain and Germany-listed shares takes place outside the respective exchanges.³²

At one point, the creation of a transatlantic exchange in the form of NYSE-Euronext was viewed as a threat to the Asia-Pacific exchanges, which risked losing both issuers and traders.³³ This did not occur, however, primarily due to a number of the Asian exchanges remaining independent.

²⁵ Ibid.

²⁶ Ibid.

²⁷ Gorham and Singh, above n 4, 125.

²⁸ ‘New York Stock Exchange and Euronext Merge’, *The Guardian* (online), 2 June 2006 <<https://global.factiva.com/>>.

²⁹ Schammo, above n 1, 827.

³⁰ Pan, above n 18, 134.

³¹ Ivan Png and Chi-Wo Cheng, ‘Merge or Bust for Local Bourses’, *Financial Review* (online), 15 June 2006 <<https://global.factiva.com/>>.

³² Ibid.

³³ Ibid.

The merger of NYSE and Euronext was intended to truly internationalise the NYSE, and in the process, create the world's largest stock market,³⁴ in terms of the value of and geographic reach of the two companies.³⁵ At the time of the merger, it would have a market capitalisation of over US\$20 billion,³⁶ which would be US\$6 billion more than that of Deutsche Boerse and \$7 billion than CME.³⁷

A number of reasons were put forward to justify the merger.³⁸ Potential investors would have access to stocks in both the United States and Europe, and at better prices despite the fact there would not actually be dual-listing.³⁹ A merger would also help NYSE recoup lost revenues resulting from a decline in listings and initial public offerings attributed to the complexity of US securities law. There was 'growing interest of US investors for foreign securities, but also as a result of a general feeling that US regulatory requirements are at the expense of the competitiveness of US securities markets'.⁴⁰ In particular, the complexity of US securities law discouraged foreign participants from entering the US market. The NYSE Euronext merger was looking for extra market and regulatory space.⁴¹

The NYSE lacked a derivatives trading platform, a second motivating factor in the merger. The success of LIFFE in London, had not been lost on the NYSE. Derivatives trading, and its profitability, were skyrocketing. Finally, a merger presented opportunities for cost cutting through technology sharing and reductions in staffing.⁴²

But the disparity in revenue growth between stock and derivative exchanges was key.⁴³

	Stock exchanges	Derivative exchanges
Revenue growth	10-15%	20-30%

³⁴ 'New York Stock Exchange and Euronext Merge', above n 28.

³⁵ Gorham and Singh, above n 4, 169.

³⁶ Howard Packowitz and Stephen Wisniewski, 'CME Seen Keeping Cautious Course Despite NYSE-Euronext', *Dow Jones Newswires* (online), 22 May 2006 <<https://global.factiva.com/>>.

³⁷ 'There are persuasive aspects of the merger plan that Thain presented. NYSE Euronext's pro forma market capitalization of \$21 billion would be \$6 billion to \$7 billion bigger than that of Deutsche Borse or Chicago Mercantile Exchange Holdings' in Jeffery Kuller, 'Hurry Up and Slow Down', *Securities Industry News* (online), 29 May 2006.

³⁸ Roberta S Karmel, 'The Once and Future New York Stock Exchange: The Regulation of Global Exchanges', (2006) 1 *Brooklyn Journal of Corporate, Financial & Commercial Law* 355, 357.

³⁹ Ibid.

⁴⁰ Schammo, above n 1, 827-828.

⁴¹ Ibid 827, 828 n 4. This problem has been raised by commentators previously and acknowledged by Schammo.

⁴² Karmel, above n 38, 357.

⁴³ Lees, above n 10, 59. Author's estimates, taking into account the statement by Terry Duffy, chairman of CME Group at Midwest Finance Association Luncheon, 6 March 2009 in Chicago, Illinois.

Operating profit margin	15-20%	40-60%

At the time, NYSE CEO John Thain anticipated the merger would bring benefits valued at US\$375 million to the group, US\$275 million of which through economies associated with greater efficiencies in the trading systems,⁴⁴ by combining IT systems and the nine data centres of the two exchanges.⁴⁵

Further, the merger would allow the new business to introduce new derivatives and futures products as well as satisfying European demand for Euro-denominated US equities.⁴⁶ Euronext.Liffe was an established brand name in the derivative markets already.⁴⁷ The success of the Euronext's derivatives business and its fixed income platform (MTS) co-owned with Borsa Italiana made Euronext, supposedly, more attractive to the NYSE than a deal with the LSE.⁴⁸ In any event, the LSE was off the table; Nasdaq, the NYSE's arch competitor, held more than a 25 percent stake in LSE.⁴⁹

2 Why Euronext Preferred NYSE?

For Euronext, the choice was between NYSE and Deutsche Börse but NYSE offered 'more investors, alternative listing opportunities, a better payout, and possibly easier regulation'.⁵⁰ A 'merger of equals' with the NYSE, rather than a takeover by Deutsche Börse, seemed the better offer.⁵¹ NYSE also assured Euronext that there would be no interference by the Sarbanes-Oxley legislation or the US Securities and Exchange Commission. A merger with NYSE would leave Euronext 'wholly in charge of European operations in a combined company'.⁵²

The 'a merger of equals' meant Euronext would be able to maintain 'independence of all exchanges involved as well as the flexibility necessary to preserve Euronext's federal and

⁴⁴ Gorham and Singh, above n 4, 169 n 18 (National Posts financial Post and F.P. Investing, 8 June 2006, 10).

⁴⁵ 'London Listings Threat from NYSE/Euronext Merger', *Citywire* (online), 22 May 2006 <<https://global.factiva.com/>>.

⁴⁶ Ibid.

⁴⁷ James Quinn, 'Stock Exchanges London's Name Counts, Even for the NYSE-Euronext Deal', *The Daily Telegraph*, 5 June 2006 <<https://global.factiva.com/>>.

⁴⁸ Ibid.

⁴⁹ 'Stockwatch LSE Dips on News of Proposed NYSE/Euronext Merger UPDATE', *AFX Asia* (online), 22 May 2006 <<https://global.factiva.com/>>.

⁵⁰ Christopher Osborne, 'A Look at the Globalization of the Exchanges and Its Effects on the United States Market Through an Analysis of the NYSE and Euronext Merger', (2008) 1 *Journal of Business, Entrepreneurship and the Law* 447, 454.

⁵¹ Lees, above n 10, 106

⁵² Anju Gagahar, 'A \$14 bn Deal was Won by Compromise', *Financial Times* (online), 23 December 2006 <<https://global.factiva.com/>>.

horizontal business model'.⁵³ Euronext headquarters would stay in Paris, rather than being moved to Frankfurt as contemplated by the Deutsche Börse,⁵⁴ The NYSE could move faster than Deutsche Börse too, with completion within six months, rather than the year needed by Deutsche Börse due to the antitrust concerns associated with concentration of the derivatives markets.⁵⁵

Also, LIFFE supported the NYSE proposal; the City of London was afraid LIFFE would be disbanded with its expertise relocated to Frankfurt. With NYSE acquiring Euronext, LIFFE would be able to draw on the deep pool of equity of the merged group to strengthen London's position as a derivatives centre.⁵⁶

3 *Merger of Equals*

NYSE signed a combination agreement with Euronext on 1 June 2006,⁵⁷ a 'merger of equals', with equal shareholder contributions and a fully balanced governance structure.⁵⁸

4 *Pre-Merger Concerns*

(a) *Regulatory Framework*

There was no precedent for a transatlantic exchange; how could a cross-border exchange, operating in multiple time zones, jurisdictions and asset classes, be regulated.⁵⁹ Differing regulatory approaches and techniques were likely to set US and European regulators at odds.⁶⁰

The SEC began talks with the then UK Financial Services Authority to discuss 'the implications of cross-border exchange mergers' and other "common areas of regulatory interest'. The two regulators spoke vaguely of promoting high standards and strong investor protection,⁶¹ but the roles of different regulators in the post- merger environment remained

⁵³ Osborne, above n 50, 456 n 88.

⁵⁴ Ibid.

⁵⁵ Alistair MacDonald, Jason Singer and Edward Taylor, 'NYSE Mega-Merger Gets Closer', *The Wall Street Journal* (online), 24 May 2006 <<https://global.factiva.com/>>.

⁵⁶ Peter Kim, 'Developments in Banking and Financial Law: 2006-2007: X. Securities Exchange Merger Activity' (2007) 26 *Annual Review of Banking & Financial Law* 85, 88-89.

⁵⁷ 'Event Brief of NYSE Group Merger & Acquisition Announcement Event – Final', *Voxant FD (Fair Disclosure) Wire*, 2 June 2006.

⁵⁸ Ibid.

⁵⁹ Tobias Buck and Jeremy Grant, 'Proposed Deal would Outstrip Regulators', *Financial Times* (London), 22 May 2006, 30.

⁶⁰ Ibid.

⁶¹ Jeremy Grant, 'US and UK Regulators Hold Talks', *Financial Times* (online), 3 June 2006 <<https://global.factiva.com/>>.

unresolved. Futures industry regulators had already addressed these issues, partly prompted by efforts by Eurex and Euronext-Liffe to compete against Chicago's exchanges. The combined NYSE/Euronext holding company would be regulated by the SEC, that was clear, although not as an exchange, but Euronext's component stock exchanges would continue under local regulatory supervision.

Nonetheless, questions remain over what role the SEC may have, if any, in European jurisdictions in the event of systemic failures, insider trading, bankruptcies or frauds.⁶²

Accounting issues, listing standards and the applicability of the controversial Sarbanes-Oxley legislation in the United States also remained unresolved.⁶³ Nevertheless, regulatory approvals were expected within six months from both sides of the Atlantic.⁶⁴

The anglo-american model of the exchange as a self-regulatory organisation (SRO) proved particularly problematic. The NYSE had been rocked by scandal in the early 2000s. After the Arca merger, a new entity, NYSE Regulation Inc, was set up as a separate not-for-profit subsidiary of NYSE Group to perform the regulatory function of the SRO, including listed company compliance, member firm regulation, market surveillance, enforcement and dispute resolution.⁶⁵

(b) Opposition to the Merger

Major shareholders in some of the biggest European exchanges' opposed the merger, preferring the advances of the Deutsche Börse.⁶⁶ Markets are sensitive to cultural, not just monetary, forces, as exemplified by the long history of failed LSE mergers.⁶⁷

Markets are cultural, not monetary and each is distinct. Not to worry, Mr. Thain says — Euronext will survive as a distinct entity. He should worry, because if French economy minister Thierry Breton has his say, this merger will not proceed without guarantees that the Euronext Paris headquarters will be preserved in aspic for generations to come. Indeed, if NYSE wants to wrap the world in Wall Street, it should think very hard about whether it is doing the right deal.

Two decades ago, U.S. and European banks flocked to the City of London to buy old broking and stock jobbing firms whose monopoly and restricted practices were being exploded in London's stock market deregulation — the Big Bang. The partners of venerable firms walked

⁶² Ibid.

⁶³ Buck and Grant, above n 59.

⁶⁴ Anju Gagahar, 'Thain Sees Agreement in "Days"', *Financial Times* (online), 2 June 2006 <<https://global.factiva.com/>>.

⁶⁵ Karmel, above n 38, 388.

⁶⁶ 'Euronext, NYSE Set to Unveil 20 Bln Dlr Merger: Report', *Agence France Presse* (London), 21 May 2006.

⁶⁷ Kulter, above n 37. 'The managements of Deutsche Borse and the LSE agreed to a merger. Then they had to fight the distraction of a self-styled white-knight bid for London by OM Group, the Stockholm-based cross-border exchange operator and technology purveyor now called OMX. But the idea was finally killed by rank-and-file Londoners who couldn't abide foreign ownership'.

away with millions.

What did the bankers buy? They bought a lad with a book. In the dying weeks of the old London Stock Exchange, I spent a few days on the trading floor watching a stock jobber, a lad with a stubby pencil, scribble entries into a large black ledger, using mental arithmetic to calculate his long or short position at frightening speed.

The bankers bought the book, not the lad, and that was their mistake. It led to torrents of red ink post-Big Bang as supposedly sound businesses faded into oblivion when the rules of the game changed. The rules are changing again. In an electronic world, stock exchanges are an anachronism. Increasingly, the investment banks of the City of London are internalizing share trading, running books on big company stocks in-house rather than through the London Stock Exchange. This will grow in importance, raising the question: what is the LSE?

Whatever it is, the foolish Nasdaq has bought 25 per cent of it and NYSE is bidding €8-billion for Euronext — another set of rules and a bank of computer servers. In the end, NYSE is also buying into a separate risk — a new culture of regulation. It is the failure of the U.S. legal system that is driving NYSE overseas. The sharpened regulatory teeth of Sarbanes-Oxley have been a disaster for Wall Street — American corporate financiers have watched aghast as foreign issuers flock to Europe, forgoing NYSE's big board in favour of the less prescriptive listing rules of the LSE. The effect of Sarbanes-Oxley is to preclude one-half of a NYSE-Euronext merger; American investors cannot access the European listings of the merged bourse for fear of incurring the wrath of the Securities and Exchange Commission.

Can NYSE, the standard bearer of U.S. capitalism, feel at ease in continental European markets with their parochial nationalism and aversion to hostile takeovers? It must be doubtful. In the end, NYSE will learn the hard way that markets succeed not on price but on confidence. Markets are where like-minded people feel happy doing business with each other. It's that simple.⁶⁸

The success of a cross-border merger is 'more a matter of politics and regulation than business exigencies and is therefore difficult to predict'.⁶⁹ Exchanges are national symbols. John Thain, the CEO of the NYSE, insisted on the necessity of change. 'Most countries have an army, a flag, an airline and an exchange. As the markets have become more global, that nationalist tendency on the part of exchanges—at least those that want to compete globally--has to break down'.⁷⁰ Even the supposed cost savings of the proposed merger were questionable; integrating trading platforms was a formidable, time-consuming task.⁷¹

The French government had long resisted foreign takeovers, for example the possible takeover of the foodgroup Danone by the Pepsi.⁷² 'Euronext has been more anxious to fend off advances from its Frankfurt rival Deutsche Börse. Under yesterday's deal, the NYSE will

⁶⁸ Abstract from Carl Mortished, 'Bourses Do Their Bidding Unaware of What a Market Is', *The Globe and Mail*, 25 May 2006, B15.

⁶⁹ Karmel, above n 38, 355.

⁷⁰ Aaron Lucchetti, 'Big Board Sees a Bond Bonanza', *Wall Street Journal* (online), 21 June 2006 <<https://global.factiva.com/>>.

⁷¹ Kulter, above n 37.

⁷² Julia Kollwe, "'NYSE-Euronext Merger' a Blow Against French Protectionism', *The Independent*, 3 June 2006, 46.

buy Euronext for about EUR7.8bn (£5.4bn). While the senior roles within the new NYSE Euronext are carefully balanced, NYSE shareholders will have a majority of the capital of the combined company. It will be based in New York, while London will be home to the derivatives business.’

In Paris, opposition to the merger has mounted. An influential lobby group, Paris Europlace, which promotes the French capital as a financial market, raised concerns related to market liquidity and safeguarding a European legal and regulatory framework.⁷³ Paris Europlace commissioned a report to study alternatives. France’s biggest bank, BNP Paribas, also opposed the merger, despite being an advisor to Euronext on the merger.⁷⁴ The BNP Paribas owned 1% and was member of shareholder voting group controlling 10% of Euronext. Other members in the voting group included Societe Generale, Dexia, and Credit Agricole.⁷⁵ The opposition from BNP Paribas was said to be heavily influenced by its chairman, one of the most influential bankers in France, Mr Pebereau, who had taken a pro-European stance favouring a Euronext - Deutsche Börse merger.⁷⁶

On the other side of the Atlantic, NYSE shareholders worried that the NYSE needed more time to adjust to its new status as a public company and to fully digest the Arca acquisition.⁷⁷ Also, differences in management policies were a concern; Euronext paid dividends, for example, while NYSE did not.⁷⁸

(c) *The Impact of US Securities Law*

The very real potential for regulatory spill-over from the US worried European regulators and industry participants. For that reason, the transaction was structured so that each market would continue to be locally regulated.⁷⁹ European companies had long protested extraterritorial aspects of the 2002 Sarbanes-Oxley legislation. US House Financial Services Committee Chairman Oxley supported the merger, from a US perspective, while defending

⁷³ ‘French Lobby Group: Euronext-NYSE Deal Raises Questions’, *Dow Jones International News* (online), 2 June 2006 <<https://global.factiva.com/>>.

⁷⁴ Martin Arnold, ‘BNP Paribas Opposes Merger Proposal: NYSE-Euronext Linkup; One of Four Banks Advising European Exchange’, *Financial Times* (online), 5 June 2006 <<https://global.factiva.com/>>.

⁷⁵ Ibid.

⁷⁶ Ibid.

⁷⁷ Shawn McCarthy, ‘Transatlantic Exchange Deal Faces Rough Sail’, *The Globe and Mail*, 3 June 2006, B3.

⁷⁸ Gaston Ceron, ‘NYSE CEO: Euronext Merger Plans in Early Stage’, *Dow Jones Newswires*, 1 June 2006.

⁷⁹ ‘New York Stock Exchange and Euronext Merge’, above n 28; Arnold, above n 74.

the investor protections provided by the Sarbanes-Oxley legislation.⁸⁰ On June 2, 2006, the House Financial Services Committee of the United States issued the following statement:

Yesterday's announcement of the merger of NYSE Group, Inc. and Euronext NV launches the NYSE to a new level of global leadership in the capital markets. This next challenge for the NYSE will continue to foster technological innovation. American investors will benefit from an improved competitive position for U.S. financial services companies in the global markets.

It's important to note that the merger will not undermine Sarbanes-Oxley protections for investors in U.S.-listed firms, and those protections will remain the same. At the same time, I expect the new alliance and additional trading platforms, as joined with the NYSE, will strengthen and deepen one of America's most critical marketplaces.

Equally as challenging as the NYSE's initiative will be the multi-national regulatory effort that has already begun at the Securities and Exchange Commission. The international regulatory bodies will need to be as vigorous as the markets they oversee.

Investors and public companies should look forward to the world's first transatlantic exchange.⁸¹

(d) *Implications for the LSE*

Speculation was rife that the LSE was next. With its less stringent regulatory approach, the LSE had been attracting listings away from the NYSE. The LSE was somewhat scornful of a potential takeover by the new NYSE Euronext.⁸² NYSE CEO Thain did not dismiss the possibility, despite Nasdaq's 25% interest in the LSE, but indicated that he preferred setting up a rival exchange in London.⁸³ The LSE laughed off such a move.⁸⁴

(e) *Bid from Deutsche Börse*

The Deutsche Börse had suffered from a number of setbacks in its attempts to acquire the LSE. In the face of the NYSE Euronext merger announcement, Deutsche Börse mounted a campaign to discourage Euronext shareholders from voting for it.⁸⁵ Deutsche Börse had proffered a higher bid for Euronext in June 2006, in the hopes of spinning off the Euronext technology to a joint venture with Atos, a European IT services corporation, and promoting its own subsidiary Eurex for derivatives trading.⁸⁶ In the proposal, Euronext would appoint the chairman and Deutsche Börse the CEO of the new entity.⁸⁷ Competition concerns among

⁸⁰ 'Rep Oxley Issues Statement on NYSE, Euronext Merger', *US Fed News*, 2 June 2006.

⁸¹ *Ibid.*

⁸² 'NYSE-Euronext Merger Could Lead to New Stock Market in London, NYSE Chief Says', *Associated Press Newswire*, 19 June 2006.

⁸³ *Ibid.*

⁸⁴ *Ibid.*

⁸⁵ 'NYSE-Euronext Merger Would Boost France's Financial Role: NYSE Chief'

⁸⁶ 'Deutsche Borse New Euronext Bid – NYSE Announcements', *Banking Newslink*, 20 June 2006.

⁸⁷ *Ibid.*

regulators, investment banks, institutional brokers and major corporates around the world ultimately scuppered the deal. It was terminated in November 2006.⁸⁸

(f) *Antitrust Concerns*

Britain's Office of Fair Trading invited comments on whether the NYSE-Euronext tie-up could lead to substantial lessening of competition in UK markets, as Euronext owned the Liffe derivatives exchange and the exchange would be the center of the merged group's derivatives business.⁸⁹ In June 2006, it was referred to the UK Competition Commission for investigation and report, although the UK implications were tenuous.⁹⁰

5 Events that Led to the Completion of the Mergers

(a) *Compromise and Strategic Moves by the NYSE*

Vocal opposition to the merger resulted in compromises on the part of the NYSE. Originally, the governance structure contemplated a 20 member board with the NYSE holding 11 seats and Euronext nine.⁹¹ By November 2006, NYSE gave way and announced that the board of the merged entity would consist of twenty-two members, equally split between NYSE and Euronext.⁹² Goldman Sachs, a heavyweight mergers and acquisition advisor, was appointed to as advisor to both entities. The NYSE also engaged French advisor, Societe Generale to appeal to the European community:⁹³

Having Societe Generale in its corner also could help the NYSE score points and soothe egos elsewhere in Europe, where a merger with a U.S. financial institution can be a politically sensitive subject. Tuesday, French President Jacques Chirac said he favored a 'Franco-German solution' for Euronext, a reference to Deutsche Boerse AG (DB1.XE), the German exchange operator that remains interested in Euronext and could be a threat to the NYSE's plans. But Chirac also conceded that politicians have little power to intervene in the deal.⁹⁴

(b) *Pre-Merger Declines in Share Price Adversely Affects the Merger*

With the announcement of the transaction, exchanges in the US and in the EU experienced declines. Euronext's shares dropped about 7%. But NYSE's shares slid some 20%, devaluing the "currency" of NYSE's contribution to the merger (which was comprised of cash and

⁸⁸ Kim, above n 56, 87.

⁸⁹ Lydia Adetunji, 'OFT Invites Comment on NYSE-Euronext Merger Plan', *Financial Times*, 16 June 2006.

⁹⁰ 'Britain's Competition Watchdog Considers Probe into NYSE-Euronext Merger', *Associated Press Newswires*, 16 June 2006.

⁹¹ Aaron Lucchetti, Alistair Macdonald and Kara Scannell, 'NYSE, Euronext Merger Set to Form Market Giant', *The Wall Street Journal*, 2 June 2006.

⁹² Kim, above n 56, 87.

⁹³ Gaston Ceron, 'NYSE Taps Societe Generale as Advisor on Euronext', *Dow Jones News Service*, 7 June 2006.

⁹⁴ Ibid.

shares). Suddenly, the Deutsche Börse proposition looked much more attractive to Euronext.⁹⁵

(c) Clarification of Concerns over the Extraterritorial Application of US Law

Both US courts and regulators are notorious for the extraterritorial application of US law. To assuage European fears, the SEC released a statement to the effect that US securities law would not apply to the European entities in the merger provided they did not list or do business in the US. In particular, the expense and aggravation associated with compliance with the requirements of the 2002 Sarbanes-Oxley legislation was a particular thorn in the side of European companies, prompting en masse departures from US markets. These defections had been an embarrassment to the SEC and it quickly moved to reassure Euronext that merger ‘would not result in the mandatory registration of a non-US exchange’s listed companies with the SEC or the mandatory compliance with the provisions of the federal securities laws, including the Sarbanes-Oxley Act, that would derive from that registration’.⁹⁶

(d) Sidestepping US Regulators

Despite assurances from the SEC, elaborate structural precautions were taken on the European side to avoid tripping US regulatory triggers. Euronext planned to create special trusts to hold operating licences granted by European regulators to its European exchanges, shielding them from unwanted (or unwarranted) US regulatory attention. Voting rights would be split off from the economic interests vested in the group holding company.⁹⁷

In that deal, the corporate holding company owned depository receipts in a trust carrying the economic rights, but not the voting rights, of an underlying trust. The licences of the exchanges, which are granted by regulators in each country in which Euronext operates, would be vested in the trusts.⁹⁸

A group of ‘wise men’ would be appointed to guard against the interest of these trusts which would require them to vote collectively in the event the European exchanges became subject to US regulation.⁹⁹ This kind of structure had been adopted before in major European

⁹⁵ John Authers, Jeremy Grant and Norma Cohen, ‘SEC Moves to Ease European Fears over Regulation’ *Financial Times*, 16 June 2006.

⁹⁶ Ibid.

⁹⁷ ‘Euronext Mulls Trust to Sidestep US Regulators’, *Reuters News* (online), 27 June 2006; Norma Cohen and John Authers, ‘Euronext Protects Itself from US Rules’, *Financial Times* (online), 27 June 2006 <<http://www.ft.com/cms/s/0/add1654c-060f-11db-9dde-0000779e2340.html>>.

⁹⁸ Cohen and Authers, above n 97.

⁹⁹ Ibid.

mergers sensitive to national interests, for example in the case of Air France and KLM Royal Dutch Airlines.¹⁰⁰

(e) Memorandum of Understanding between the SEC and the Euronext College of Regulators

In the absence of an overarching transatlantic regulatory framework, in January 2006 the SEC entered into a Memorandum of Understanding with the Euronext College of Regulators to facilitate cooperation in the oversight of NYSE Euronext.¹⁰¹ Market participants responded positively, recognizing the commitment on the part of the SEC to communicate and coordinate with other financial regulators, so as to reduce the complexity and costs of compliance of multiplicity of regulatory regimes.¹⁰²

III AN OVERVIEW OF THE MERGED NYSE EURONEXT GROUP¹⁰³

Under the NYSE Euronext Group, there were two main subsidiaries – the NYSE Group Inc located in the U.S. and the Euronext N.V., a Dutch corporation, in Europe. The NYSE Group Inc had four subsidiaries, NYSE, NYSE ARCA, NYSE ARCA Options and ArcaEdge. At the time, the NYSE still had a traditional trading floor together with a new electronic bond trading platform. NYSE ARCA (previously the Archipelago Exchange) provided an electronic platform for NYSE listed stocks and ETFs as well as those of rival exchanges, AMEX and Nasdaq. NYSE Arca Options had both an electronic platform and a trading floor in San Francisco. Lastly, ArcaEdge traded small, unlisted stocks on its platform.

On the other side of the Atlantic, Euronext N.V. had six main subsidiaries, namely, Amsterdam Exchange, Lisbon Exchange, Paris Bourse, Brussels Exchange, NYSE Alternext Equities and London International Financial Futures Exchange (LIFFE). The four Euronext exchanges in Amsterdam, Lisbon, Paris and Brussels all traded both stocks and derivatives. At the time, LIFFE was the fourth largest derivatives exchange in the world after the CME in Chicago, the Korea Exchange and Eurex. Mimicking the LSE's Alternative Investment Market (AIM), NYSE Alternext provided a lightly regulated trading platform for small and medium-sized companies in France, Belgium and the Netherlands.

A Post-Merger

¹⁰⁰ Ibid.

¹⁰¹ Giovanni Prezioso, 'The Race to Optimality' (2007) 66 *European Lawyer* 3, 3.

¹⁰² Ibid.

¹⁰³ Gorham and Singh, above n 4, 171.

Once the merger was completed, listing and market data each contributed about 17% of the revenues for NYSE Euronext. At 26%, derivatives trading constituted the largest single source of revenues. In 2009, with the rise in demands produced by high frequency trading, NYSE-Euronext set up two major data centres, one in London and another one close to New York City, saving US\$30 million a year in operating costs.¹⁰⁴ Cutting costs was imperative on the NYSE side. Given the highly competitive environment in which they operate, US exchanges have surprisingly low profit margins, 9% and 8% for the NYSE and NASDAQ, respectively, in 2005 and 2006,¹⁰⁵ placing them fifth and eighth among the twelve largest exchanges in the world.¹⁰⁶

B Reactions to the Merger

*1 No Perceived Threats in the Short Term*¹⁰⁷

Given the strong profitability of Deutsche Börse in particular (greater than that of NYSE and Euronext combined), the merger appeared to pose little threat to European exchanges in the short term.

The competitive threats from NYSE Euronext are really medium- to long-term threats”, said Andrew Mitchell at brokerage Fox-Pitt, Kelton. That's because snatching liquidity away from an incumbent exchange is extremely difficult, Mitchell said. Once trading is focused in one particular exchange, it is hard for another bourse to attract it elsewhere.

Although it's possible that the new NYSE Euronext may entice away companies that would once have listed on the LSE, analysts said admission fees from new listings are actually a small part of the revenues of both the London exchange and Deutsche Boerse.

Admission fees from companies listing on the main market and on the Alternative Investment Market, or AIM, made up just 9% of LSE's full-year revenues in fiscal 2006, according to one analyst's estimate. Trading equities and data services alone made up three-quarters of full-year sales.

¹⁰⁴ Jonathan Spicer, 'NYSE Aims for Human Touch as it Modernizes', *International Herald Tribune*, 5 August 2009, 15.

¹⁰⁵ (2008) 3(1) *Journal of Trading*, 126.

¹⁰⁶ Lees, above n 10, 65.

¹⁰⁷ Nichole Lee, 'Focus: Europe's Exchanges Should Resist Urge to Merge', *Dow Jones International News*, 2 June 2006.

Most of Deutsche Boerse's revenues come from its Eurex derivatives arm and its Clearstream clearing and settlement business, with only 0.8% coming from listing fees, a spokeswoman for Deutsche Boerse said.

"The long-term benefit of attracting large volumes of new listings is that it generates more trading because it increases the amount of market capitalization that you have. Ultimately that's more important than any initial boost from admission fees," Fox-Pitt, Kelton's Mitchell said.

Although the range of options has narrowed now that Euronext and NYSE are moving one step closer to a merger, for now Europe's exchanges still have partners to choose from, analysts said.

Lynton Jones, partner at Bourse Consult, a stock exchange consultancy based in London, said an LSE deal with the Swedish exchange operator OMX AB (OMX.SK) is one possibility, while a three-way tie-up involving Deutsche Boerse, the LSE and Nasdaq is still another possibility.

Nonetheless, "it is true to say the position of the LSE has been weakened" since a NYSE-Euronext merger removes two potential bidders from the LSE's list of suitors, Jones said.

Deutsche Boerse could forge its own transatlantic deal with the Chicago Mercantile Exchange, another analyst said. Also, the chief executive of the Vienna Stock Exchange expressed willingness Friday to start exploring ways it might cooperate with Deutsche Boerse.

In the meantime, NYSE Euronext is already advancing on other bourses. Borsa Italiana SpA, the privately held operator of financial exchanges in Milan, confirmed Friday that it is in talks with NYSE and Euronext about joining the merged company.

C Benefits of the Merger

*1 Long Term Gain*¹⁰⁸

¹⁰⁸ Brooke A Masters and Paul Blustein, 'NYSE in Europe? Investors Won't Notice Much Change at First', *The Washington Post*, 11 June 2006, F01.

The merger was more about a long term gain rather than short term promise, by providing investors with new investment options and lower transaction costs; it changed remarkably little. A new holding company sat above different, existing, markets; equities in New York, Lisbon, Amsterdam, Paris and Brussels; derivatives in London; and a cash and options market on the electronic platform of Archipelago.

Importantly, except for cross listed securities, the new structure did not provide US retail investors access to European stocks. Although there was no formal legal impediment to US retail investors acquiring foreign shares, industry mandated investor suitability requirements would deter their sale by US brokers. In the longer term, retail investors might have been able to diversify their holdings through exchange traded funds which would include Euronext shares, derivatives and options contracts. In theory, lower transaction costs would also be available to them.

This first transatlantic merger was expected to lead to ‘a more globally integrated securities market’¹⁰⁹ but fell far short of a revolution in exchange trading. The NYSE and Euronext markets could not be integrated due to European wariness of the potential applicability of US securities laws.

2 Round the Clock Trading

Both Euronext and NYSE Arca planned to operate 22 hours a day, opening the door to increased cross-border trading between US and European stocks and derivatives and arbitrage opportunities.¹¹⁰ However, it was unclear which electronic trading platforms would be open to US investors to access a proposed global consolidated marketplace. The benefit of having a new consolidating NYSE and Euronext’s trading systems would benefit multi-asset trading.¹¹¹

3 Dual Listing and Why it Didn’t Materialise

One benefit originally touted prior to the merger itself was the opportunity for investors to trade in both the US and Europe. Sarbanes-Oxley had driven big European issuers off the NYSE as well as deterring new listings by non-US issuers. The NYSE saw the merger as a way of recouping lost ground. For example, in 2005 London exchanges raised over \$10.3 billion in foreign IPOs compared to \$6 billion in the US. Only two out of the 25 international

¹⁰⁹ Ibid.

¹¹⁰ Ivy Schreck, ‘What Does NYSE-Euronext Mean for the US Trader’, *Wall Street + Technology* (online), 1 July 2006.

¹¹¹ Ibid.

IPOs were listed on US exchanges.¹¹² But the merger of NYSE and Euronext did not result in automatic dual listing of US and European issuers. Regulatory compliance costs and the threat of class action litigation in the US had not abated.

IV A REGULATORY DILEMMA AND ITS CRITICS

The NYSE-Euronext merger created a regulatory dilemma: how do jurisdictionally bound regulators regulate a transatlantic, multijurisdictional exchange. Deregulation and demutualisation had galloped in tandem around the globe.¹¹³ However, deregulation did not mean ‘no regulation’. Rather it led to a different regulatory logic, especially in face of the assault on the territoriality principle of regulation mounted by electronic trading.¹¹⁴ ‘Physical distance is becoming meaningless’¹¹⁵ due to the introduction of electronic trading platforms. Trading takes place in a space of flows.¹¹⁶ Data, information, orders and capital are all flowing from different geographical locations mindless of territorial boundaries.¹¹⁷ When ‘regulators seek to grapple with this cross-border organization of market space, the organization of the regulatory space is increasingly being challenged for its lack of fit’.¹¹⁸

Differences in regulatory techniques and approaches as between the US and Europe were an obvious problem in regulating a transatlantic exchange. Less obvious were the differences in regulatory attitudes between the two domestic US regulators, the SEC and CFTC. The SEC had long taken a restrictive approach to market access; foreign exchanges setting up direct trading facilities in the US had to be SEC registrants, subject to the whole panoply of US securities regulation.¹¹⁹ The CFTC had been more accommodating, deferring to home country regulators and permitting relatively open access to US markets. The burgeoning derivative exchanges did not face the same legal hurdles as European stock exchanges in terms of entering the US markets.¹²⁰

The merger of NYSE and Euronext put squarely into question the applicability of US securities law to the new entity.¹²¹ In the aftermath of the controversies surrounding the

¹¹² Karmel, above n 38, 363.

¹¹³ Schammo, above n 1, 833.

¹¹⁴ Ibid 833-834.

¹¹⁵ Ibid 833.

¹¹⁶ Ibid 833 n 21.

¹¹⁷ Ibid 833 n 23.

¹¹⁸ Ibid 833.

¹¹⁹ Ibid 837.

¹²⁰ Ibid 829.

¹²¹ Ibid 836.

application of the notoriously unpopular Sarbanes-Oxley Act to European issuers,¹²² the restrictions on market access postulated by the SEC, garnered intense scrutiny by the EU.¹²³ The merger was no routine commercial event, but one heavy in political consequence.

Without regulatory compromise or harmonised approaches, the realisation of a transatlantic exchange remained illusory. In addition to lower operating costs resulting from shared technology platforms through sharing platforms and other resources, the greater liquidity produced by larger trading pools was the goal of the merger. It did not materialise.

At the heart of the difficulties was the Memorandum of Understanding (MOU) between the regulators on each side of the Atlantic. Memoranda of understanding are administrative instruments, useful in non-contentious situations, but lacking strong legal authority. The regulators party to the NYSE-Euronext MOU endeavoured to ‘harmonize the legal frameworks of each country to promote the stock market integration.’ However, the disparities of accountability standards, reporting and corporate governance requirements and disclosure systems proved impossible to overcome.¹²⁴

Shipp also criticised the MOU entered into by the SEC in relation to regulating the NYSE Euronext Group, which excused itself from any legal obligations on the SEC to enforce securities law provisions and carry out investigation or bringing litigation on potential violations of securities law.¹²⁵ The MOUs entered by SEC in substance agrees to information sharing arrangements.¹²⁶ Rather, these MOUs contain provisions which give the SEC power to ‘conduct on-site visits in the territory of a foreign jurisdiction to ensure compliance with ongoing obligations under US securities laws.’ This instead has extended the power of SEC to have direct access to foreign firms’ records should it be subject to the compliance of US securities law.¹²⁷ Shipp argues that the MOUs ‘do not contemplate coordination or convergence in securities regulation proper’.¹²⁸

Shipp contrasted the MOUs executed by the US to the MOU created for regulating Euronext. The Euronext Regulatory MOU creates legal obligations on Euronext or the signatory

¹²² Ibid 840.

¹²³ Ibid 837.

¹²⁴ Dante Figueroa, ‘Integrating Latin American Stock Markets: The Mercado Integrado Latinoamericano (Mila): Innovations and Perspectives’ 3 *American University Business Law Review* 277, 281.

¹²⁵ Bryan Thomas Shipp, ‘Filling Gaps in European Union Securities Law: Contractually Organized Supervision & the College of Euronext Regulators’ (2008) 23 *American University International Law Review* 387, 417-419.

¹²⁶ Ibid 420.

¹²⁷ Ibid 421.

¹²⁸ Ibid.

authorities.¹²⁹ The MOU obligated the Euronext and Euronext College to take actions under certain circumstances. These obligations on Euronext to the Euronext College are additional to its obligations to other national authorities. This analysis highlights the different approach taken by regulatory bodies in collaborating with other authorities.¹³⁰

Shipp criticised the MOU entered into by the SEC in relation to regulating the NYSE Euronext Group in substance did not aim for ‘convergence in regulatory standards among jurisdictions’.¹³¹ He contrasted the MOUs entered by SEC with the MOU created for regulating Euronext and criticised the former lacked any enforceable legal obligations on the SEC. In situations where securities law has been breached by companies in the US, other regulators from other countries cannot rely on the MOU entered by the US and compel the SEC to bring investigation or proceedings against the violators. Whereas in the case of the Euronext Regulatory MOU, Euronext College and Euronext were obliged to take certain actions. Further, Shipp argued that there was significant power imbalance in the MOU entered by the SEC. The terms are unilaterally favourable to the US. For example, these MOUs contain provisions which give the SEC power to ‘conduct on-site visits in the territory of a foreign jurisdiction to ensure compliance with ongoing obligations under US securities laws’.¹³² This instead has extended the power of SEC to have direct access to foreign firms’ records should it be subject to the compliance of US securities law.¹³³ Shipp argues that the MOUs ‘do not contemplate coordination or convergence in securities regulation proper’.¹³⁴

V THE FAILURE OF NYSE EURONEXT

The holy grail of any transatlantic merger would be ‘one platform with a single order book’. With the NYSE Euronext merger, traders in the US and EU needed full access to listed shares in each market in order to achieve the hoped for liquidity and economies of scale.¹³⁵ It never happened. Regulatory accommodations on the US side proved too difficult to effect and burdensome SEC registration requirements continued to stand in the way of creation of a single market.¹³⁶

¹²⁹ Ibid 423.

¹³⁰ Ibid 424.

¹³¹ Ibid 417.

¹³² Ibid 421.

¹³³ Ibid 421.

¹³⁴ Ibid.

¹³⁵ Pan, above n 18, 137.

¹³⁶ Ibid 138.

At the time a breath-takingly audacious move, the NYSE Euronext merger foundered in the space of a few years. The upstart Intercontinental Exchange (ICE), an Atlanta Georgia based derivatives exchange founded barely a dozen years ago, took over and broke up NYSE Euronext in 2013. This particular dream of a transatlantic equities exchange came to an end. ICE brought the NYSE back to America. With NYSE now a subsidiary of another US regulated entity, US regulatory barriers and compliance issues melted away. The implications though have been felt strongly in Europe, and in derivatives, not equity markets, as it was reported in Financial Times:

With its baseball code words and references to icons of capitalism, the \$8.2bn ICE-NYSE Euronext deal was clearly stamped; "Made in America". But its biggest impact may be in Europe.

In announcing the deal, no one actually said it, but the sale of NYSE Euronext effectively acknowledges the 2007 merger of NYSE and Euronext has failed. The closest to admitting it was Duncan Niederauer, the chief executive brought in to run the merged business.

The market, for whatever reason, was valuing the company that we think is worth a lot more at, as you know, \$5.5bn-\$6bn. The bottom line is we had not delivered in my mind sufficient returns to shareholders," he said.

The solution proposed by Jeff Sprecher, his counterpart at ICE, was simple: a break-up of Euronext, the European assets, that would allow the ICE chief to take control of Liffe, the London interest rate derivatives exchange he has long coveted.

Ownership of Liffe will transform ICE's European business, even if ICE's London-based operations are already bigger than most realise. For example, some 65 per cent of total clearing at ICE passes through ICE Clear Europe.

It will allow ICE's global customers to trade on ICE outside US hours while also avoiding some onerous Dodd-Frank rules as they come into force in 2013. In doing so, ICE will follow the path taken by CME Group, the world's largest futures operator and the rival to which Mr Sprecher has always loved to be a gadfly.

The CME has applied to operate a full London-based derivatives exchange and expects to launch it in the second quarter. ICE Clearing Europe and Liffe already have the necessary licences. Assuming the ICE-NYSE deal closes in the second half as expected, ICE would only be a few months behind the CME.

As an aside, the ICE-NYSE deal means that Liffe will have had three new owners in just over a decade. The first, when Euronext beat the London Stock Exchange Group and Detusche Borse to the punch in 2002, valued Liffe at £555m. Its value wasn't split out in the next deal, the \$21bn NYSE Euronext merger of 2007. Interestingly, the press release at the time made no specific reference to Liffe. It may be an academic question but what price Liffe now? Half of ICE's \$8.2bn purchase price? Strip out Liffe and the assets of NYSE Euronext that remain don't look too dissimilar to either the London Stock Exchange Group or Nasdaq OMX, both valued at between \$4bn-\$4.6bn (£2.5bn-£2.9bn).

And what of the rest of the European operations set to be hived off?

Some details remain to be settled, such as the fate of NYSE's vast data centre outside London, or the future of poor Eurotunnel, the sole listing on NYSE's London listing business.

The possible flotation of Euronext is being spun as an opportunity for it to recover its independence, assuming regulatory approval. That's a likely outcome, given the paucity of possible buyers who also wouldn't run into regulatory problems. The LSE and Nasdaq OMX could struggle to raise the funds although Deutsche Börse wouldn't. But all three would face severe regulatory scrutiny from European antitrust authorities demonstrably keen to maintain competition in European equities trading.

Instead, a newly-independent Euronext is likely to be fighting for a place to dominate trading on European markets, alongside ICE, Deutsche Börse and the LSE.

As a result, it's likely to throw the future of other European bourses into sharp focus. Bolsas y Mercados Españoles is independent but faces significant new threats as European markets directives become tougher regulations. Geographically speaking, a tie-up between the Madrid exchange and the owner of the Lisbon, Paris, Amsterdam and Brussels bourses may be attractive. It would also give Euronext all-important derivatives and clearing operations.

Other questions may include: what becomes of SIX Group, owner of the Swiss Stock Exchange, and the bourses of central and eastern Europe? But perhaps the biggest is what becomes of the other main transatlantic deal - that of Nasdaq OMX?

Like NYSE Euronext, the market has a dim view of the deal - Nasdaq paid \$3.7bn in 2008 for OMX, the Scandinavian exchanges operator and the current market capitalisation of the combined company is \$4.1bn.

Nasdaq and OMX are as ill-integrated as NYSE and Euronext were. It's a state of affairs illustrated by Nasdaq's decision to build a separate London-based derivatives trading platform while also building out another European derivatives business via its stake in Holland's The Order Machine.

But like NYSE, it's hard to imagine Nasdaq's Bob Greifeld willingly spinning-off the European assets without assuaging shareholders with anything else in return. Elsewhere a newly-strengthened TMX of Canada watches on.¹³⁷

The Deutsche Börse in the picture

The Deutsche Börse experienced multiple failures attempting to acquire Euronext and NYSE Euronext. At stake has been the lucrative and growing market in financial derivatives, particularly as trading is required to move from OTC markets onto exchanges. In 2011, a consortium of ICE and Nasdaq successfully objected to the Deutsche Börse overtures to NYSE Euronext.

ICE has also become involved in the broader merger and acquisition movement in stock exchanges, which has been stimulated by the potential massive growth arising from the shift out of OTC markets. This is reflected in the bid for NYSE Euronext by Deutsche Börse in early 2011, which was accepted by the NYSE Euronext board but subsequently challenged by an alternative bid from a consortium of ICE and NASDAQ. The proposed merger later collapsed in February 2012 when the European Commission ruled that it would have created a 'near monopoly' in European financial derivatives.¹³⁸

¹³⁷ Philip Stafford, 'Quick View: Battleground Europe for Bourse', *Financial Times* (online), 31 December 2012 <www.ft.com/cms/s/0/3de68672-5333-11e2-9e71-00144feab49a.html>.

¹³⁸ Glenn Morgan, 'Reforming OTC Markets: The Politics and Economics of Technical Fixes' (2012) 13 *European Business Organization Law Review* 391, 407.

Business issues, as well as regulatory barriers, impeded the Deutsche Börse proposals, given the differences in organizational structures and disparities in the valuation of the entities.

In April 2009 the *Wall Street Journal* reported that Deutsche Borse and NYSE Euronext were in discussions on a possible deal. While it appeared unlikely the two would agree to combine in the near future, it is highly probable they will continue to study their respective options. One analyst, Diego Perfumo, observed that a joint venture limited to the derivatives and/or clearing business might be feasible as an initial step. Some doubt that significant synergistic cost savings could be gained from a merger of the two. Others argue that the size and complexity of both parties would create difficult integration issues. Valuation disparities pose an even more difficult hurdle. In April 2009 NYSE Euronext shares were valued at slightly over \$6 billion, half of Deutsche Borse's \$13 billion value.¹³⁹

Despite its numerous dalliances, Deutsche Börse has remained resolutely alone, in part due to its configuration as a vertical 'silo' integrating trading with back office clearing and settlement. The 'silo' has been a structural impediment to mergers with other exchanges (which outsource non-trading functions), but has also contributed greatly to Deutsche Börse's competitiveness and profits.¹⁴⁰

¹³⁹ Lees, above n 10, 108

¹⁴⁰ Ibid: "In this regard Deutsche Borse stood as an almost solitary figure, enjoying a profitable and large clearing facility, which tended to isolate it from the potential for merger with other leading exchanges. At that time other exchanges preferred to utilize arm's length clearing services, such as LCH.Clearnet in the case of London exchange".

A.3 THE ICEMAN COMETH – THE BIG DEAL FALLS APART

I ICE NYSE EURONEXT

The remarkably rapid rise of the IntercontinentalExchange (ICE) is symptomatic of major shifts in organised markets. Derivatives trading is eclipsing equity trading. Technology has broken down entry barriers for the creation of trading platforms. Allegiances and associations can form and shift with great rapidity. Markets morph with dazzling speed. ICE did not exist prior to May 2000 but has made at least ten acquisitions in the past 15 years. The ICE NYSE Euronext merger could be viewed as inevitable in a globalised and fragmented industry.¹ A year after a failed bid to acquire NYSE Euronext by ICE and Nasdaq OMX Group acting together, ICE successfully went it alone.²

On 20 December 2012, ICE announced its plan to pay \$8.2 million for NYSE Euronext. ICE-NYSE Euronext would be the third biggest exchanges group in the world by market capitalisation after the merger,³ behind world the Hong Kong Exchange and Clearing and CME Group.⁴ ICE was offering significantly less for the merged entity than the \$10.2 billion that NYSE paid for Euronext in 2007.⁵ The world had changed. Pre-financial crisis in 2008, the European stock markets have a much higher valuations and Liffe business was more lucrative.⁶ Profits from stock trading had been decreasing significantly due to new technology and new trading venues such as ‘dark pools’.⁷

¹ Latoya C Brown, ‘Rise of Intercontinental Exchange and Implications of Its Merger with NYSE Euronext’ (2013) 32 *Journal of Law & Commerce* 109, 119.

² ‘WSJ Blog/Deal Journal: ICE, NYSE Euronext in Talks’, *Dow Jones News Service* (online), 19 December 2012 <<https://global.factiva.com/>>. The ICE Nasdaq OMX bid did not go forward, again because of anticompetitive concerns; the US Department of Justice threatened to bring antitrust proceedings.

³ ‘Factbox-ICE-NYSE Euronext Would Go Third in World Table’, *Reuters News* (online), 20 December 2012 <<https://global.factiva.com/>>.

⁴ ‘U.S. SEC Approves ICE’s Planned Takeover of NYSE’, *Reuters News* (online), 16 August 2013 <https://global.factiva.com/>.

⁵ Luke Jeffs and Sophie Sassard, ‘Deal Talk Ice’s European Spin-off Plan Puts Euronext in Play’, *Reuters News* (online), 20 December 2012 <<https://global.factiva.com/>>.

⁶ *Ibid.*

⁷ John McCrank and Sophie Sassard, ‘ICE to Buy NYSE Euronext for \$8.2 Billion’, *Reuters News* (online), 20 December 2012 <<http://uk.reuters.com/article/2012/12/20/uk-nyse-ice-merger-idUKBRE8BJ08R20121220>>

EXCHANGE	MARKET CAP
Hong Kong Exchanges and Clearing:	\$19.5 billion
CME Group:	\$17.5 billion
IntercontinentalExchange + NYSE Euronext:	\$15.1 billion (*)
Deutsche Boerse:	\$11.7 billion
Singapore Exchange:	\$6.2 billion
London Stock Exchange Group:	\$4.9 billion

** From Reuters News⁸

II WHY ICE WANTED TO MERGE WITH NYSE EURONEXT?

Technology and globalisation have dramatically changed the stock exchange business model. Diversification has been the main strategy to boost sagging profits from the centuries old business of listing and trading financial products. ‘They’re not stock exchanges anymore’, says Peter Lenardos, analyst at RBC Capital Markets.⁹ ‘Look at the amount of money from pure cash equities, it is now in the single digits for some exchanges. It’s all about post-trading, indices, clearing. The reason exchanges continue to do well is that they have diversified. They are no longer what their names say’.¹⁰

For ICE, the most important asset in NYSE Euronext was Liffe, Europe’s second-largest derivatives market. Liffe would help ICE compete in derivatives markets against the US based CME Group, owner of the world’s largest futures market.¹¹ Derivatives trading is the modern high margin trading business for exchanges.¹²

⁸ ‘Factbox-ICE-NYSE Euronext Would Go Third in World Table’, above n 3.

⁹ ‘Exchanges Face Consolidation’, *Global Investor* (online), 1 September 2013 <<https://global.factiva.com/>>.

¹⁰ Ibid.

¹¹ Luke Jeffs, John McCrank and Jessica Toonkel, ‘ICE’s NYSE Swoop Creates Derivatives Giant’, *Reuters News* (online), 21 December 2012 <<https://global.factiva.com/>>.

¹² McCrank and Sassard, above n 7.

ICE established a clearing house in Europe – ICE Clear Europe Limited. Immediately prior to the NYSE Euronext acquisition, in December 2012, ICE Clear Europe Limited and NYX's subsidiary LIFFE Administration and Management entered into a clearing services agreement that allows ICE Clear Europe to provide clearing services to the London market of NYSE Liffe.¹³

ICE established a clearing house, and then acquired NYSE Euronext to get access to Liffe, which is the second largest derivatives exchange in Europe. So ICE plugs Liffe into its clearing house and the result is that a lot of shareholder value has been created.¹⁴

ICE, by acquiring NYSE Euronext, was able to vertically integrate Liffe with its clearing house business in Europe. Thus, the merger gave ICE, through Liffe, a powerful position in Europe's lucrative derivatives market,¹⁵ 'an about 40.3% share of the European derivatives market, compared to a 57.0% share for Deutsche Boerse AG'.¹⁶

Liffe also provided ICE with a venue for heavily traded agricultural products, including LIFFE wheat futures. Liffe competes head on with the CME Group's US-based agricultural exchange business. For example, in wheat contracts, ICE, pre-merger, had a total wheat futures volume of about 800 lots with open interest around the same level. By way of contrast, LIFFE had about 60,000 lots in wheat futures total volume with nearly 300,000 in open interest (i.e. the number of buy market orders when the stock market opens).¹⁷

The global financial crisis of 2008-09 prompted major reconsideration of the regulation of derivatives markets.¹⁸ With the introduction of the voluminous Dodd-Frank legislation in the US in 2010 and implementation of Basel III capital adequacy rules, pressures mounted to force at least part of the over-the-counter derivatives market onto exchanges.¹⁹ In particular, derivatives trading by banks have been channelled through clearing houses and regulated exchanges for in the interests of monitoring risk better, rather than permitting banks to trade

¹³ 'IntercontinentalExchange and NYSE Euronext Enter Clearing Services Agreement; ICE Clear Europe to Clear NYSE Liffe's Derivatives Markets', *Thomson Reuters ONE* (online), 20 December 2012 <<https://global.factiva.com/>>.

¹⁴ 'Exchanges Face Consolidation', above n 9.

¹⁵ Jeffs, McCrank and Toonkel, above n 11.

¹⁶ Joel Poelhuis, 'Bernstein Skeptical on ICE/NYSE Euronext Deal Pricing', *SNL Energy Finance Daily* (online), 24 December 2012 <<https://global.factiva.com/>>.

¹⁷ 'ICE, NYSE Euronext Deal Opens Energy, Equity Synergy; More Control Over Agriculture', *Platts Commodity News* (online), 20 December 2012 <<https://global.factiva.com/>>; Investopedia, *Open Interest* <<http://www.investopedia.com/terms/o/openinterest.asp>>.

¹⁸ Jeffs, McCrank and Toonkel, above n 11.

¹⁹ 'Exchanges Face Consolidation', above n 9.

directly with each other.²⁰ Exchanges liked Liffe were not slow in appreciating the opportunities this presented.²¹

III WHAT ICE HAD TO OFFER

ICE offered NYSE Euronext shareholders the market value of their shares, \$33.12 a share in cash and promised annual dividends of \$300 million (comparable to NYSE dividend payouts) to all shareholders at the time of closing of the transaction.²² ICE funded the transaction through its cash reserve and credit facilities up to 33% and the balance by issuing shares.²³

The transaction marked the end of the New York Stock Exchange's 200 years of independence.²⁴ Despite the storied history of the NYSE, and its large market capitalisation,²⁵ the exchange had been under stress due to 'heightened competition, regulatory challenges and the ongoing market volatility amid the low interest rate environment'; its global market share had shrunk from 82% to 21%.²⁶ It was time for a change.²⁷

Competition concerns were negligible and regulatory clearances uncontroversial. Unlike NASDAQ or Deutsche Börse, ICE did not have large equity operations.²⁸ The 2011 bid mounted by ICE and NASDAQ together had been stymied by the extensive overlap of Nasdaq's business with that of NYSE Euronext.²⁹ So confident were the players that the deal would sail through the regulatory approval process, that ICE agreed to a break fee of \$750 million, payable to New York Stock Exchange.³⁰

Euronext generated \$540 million in revenues for the NYSE in 2011, but ICE was not interested in Euronext's equity markets. Trading levels were declining in Europe and competition heating up with new entrants such as Bats Chi-X Europe. And, of course, there

²⁰ Jeffs, McCrank and Toonkel, above n 11.

²¹ Ibid.

²² McCrank and Sassard, above n 7.

²³ 'The Zacks Analyst Blog Highlights: IntercontinentalExchange, NYSE Euronext, Morgan Stanley, CME Group and NASDAQ OMX Group', *PR Newswire (U.S.)* (online), 24 December 2012 <<http://www.prnewswire.com/news-releases/the-zacks-analyst-blog-highlights-intercontinentalexchange-nyse-uronext-morgan-stanley-cme-group-and-nasdaq-omx-group-184676131.html>>.

²⁴ 'ICE, NYSE Euronext Faces Fees If Deal Falls Through', *Daily Tribune* (online), 23 December 2012 <<https://global.factiva.com/>>.

²⁵ NYSE has been the largest exchange in terms of the value of listing within the US, France and Netherlands; see 'The Zacks Analyst Blog Highlights: IntercontinentalExchange, NYSE Euronext, Morgan Stanley, CME Group and NASDAQ OMX Group', above n 23.

²⁶ Ibid.

²⁷ Ibid.

²⁸ McCrank and Sassard, above n 7.

²⁹ Ibid.

³⁰ Jeffs, McCrank and Toonkel, above n 11.

had been the global financial crisis.³¹ Early on, ICE announced its intention to spin off the European stock market businesses in a public offering after the merger completed.³² The market's valuation of Euronext was between 1-2 billion euros.³³

IV THE MERGER

A Changes Made to the Merger Structure

Originally, ICE had planned to acquire NYSE Euronext directly, however ultimately a new holding company structure was created with InterncontinentalExchange Group, Inc (ICE Group) at the top. Both ICE and the NYSE Euronext became wholly owned subsidiaries of ICE Group. The change was driven SEC regulatory considerations which limit the maximum shareholding level in a stock exchange by a company. The maximum shareholding level in a stock exchange differs from one exchange to another. In the case of ICE, it was 20 per cent of shareholding level in stock exchanges.³⁴ The commercial terms of the transaction, however, remained substantially unchanged.³⁵

B The Approval Process

The merger had to overcome a number of hurdles, regulatory approvals as well as shareholder approval from both entities.³⁶

1 Antitrust Clearance

Antitrust or completion concerns, as usual, were the main obstacle, triggering consideration by US and EU authorities. In the US, those authorities were the Department of Justice and the Federal Trade Commission. In the EU, the merger was subject to clearance by national competition authorities in Portugal, Spain and the UK. However, ICE and NYSE Euronext requested that the matter be referred to the European Commission pursuant to Article 4(5) of Council Regulation (EC) No. 139/2004. This mechanism streamlined the process by bypassing national authorities and the potential complication of multiple rulings.

³¹ Jeffs and Sassard, above n 5.

³² Ibid.

³³ Ibid.

³⁴ Philip Stafford, 'ICE Adjusts Terms of \$8.2bn NYSE Deal', *Financial Times* (online), 19 March 2013 <<http://www.ft.com/intl/cms/s/0/28439eaa-90c7-11e2-a456-00144feabdc0.html#axzz3tdigl1Ax>>. 'The change was made to meet requirements laid down by the Securities and Exchange Commission, which permits parties a maximum shareholding level in stock exchanges of just 20 per cent.'

³⁵ 'ICE, NYSE Euronext Tweak Merger Structure', *Reuters News* (online), 19 March 2013; 'ICE, NYSE Euronext Revise Merger Structure', *M&A Navigator* (online), 20 March 2013 <<https://global.factiva.com/>>.

³⁶ ICE, *Form S-4 Registration Statement* (25 January 2013), 122 <<http://www.sec.gov/Archives/edgar/data/1174746/000119312513024429/d461946ds4.htm>>.

2 Merger Clearance

(a) US authorities

(i) SEC

Several of the NYSE Euronext subsidiaries (New York Stock Exchange, LLC, NYSE Arca, Inc. and NYSE MKT LLC) were self-regulatory organizations (SROs) registered as national securities exchanges under US securities law and subject oversight by the SEC. Changes to SRO rules require SEC approval. Not surprisingly, the merger triggered numerous rule changes at the SRO and holding company level: amendments to the certificate of incorporation, bylaws or related documents, as well as listing and market conduct rules.

(ii) CFTC

The CFTC had to be notified in relation to the change of control of NYSE Liffe U.S., LLC as a designated contract market. The CFTC also had to approve the change of control of New York Portfolio clearing as a derivative clearing organisation.

(iii) FINRA

The Financial Industry Regulatory Authority, FINRA, is an industry association regulator. FINRA approval was required for the change in control in Archipelago Trading Services LLC and Archipelago Securities, Inc.

(b) EU Regulators

(i) Approvals from the College of Supervisors of Euronext

The merger required a declaration of non-objection from the Euronext College of Supervisors, as required pursuant to the Memorandum of Understanding between the members of the Euronext College of Supervisors dated 24 June 2010. National regulators too had to weigh in: Belgium, France, the Netherlands, Portugal, Spain, Switzerland, United Kingdom, Brazil, Hong Kong, Japan, Qatar and Singapore.

(c) Approval Timeline

The approvals started to roll in. On 19 February 2013, ICE and NYSE Euronext received the US Hart-Scott-Rodino (HSR) antitrust clearance for the \$8.2 billion merger,³⁷ as the antitrust law waiting period expired.³⁸ Following quickly was NYSE Euronext shareholder approval on 4 June 2013.

ICE chose to seek clearance from the EU competition authority, rather than approach multiple regulators in Portugal, Spain and Britain. On 24 June 2013, the European Commission cleared the deal and approved the acquisition of NYSE Euronext by ICE.³⁹ The deal did ‘not raise competition concerns as (the two) are not direct competitors in the markets concerned and would continue to face competition from a number of other competitors’, the Commission said in a statement.⁴⁰

A few weeks later, in August 2013, the SEC approved the acquisition in the US.⁴¹ Various individual financial regulators at the national level in the EU had to sign off however⁴² and the closing date was delayed a few days as the approvals trickled in.⁴³ Finally, with all approvals in hand by 10 November 2013, ICE closed the transaction three days later.⁴⁴

C Potential Benefits of the ICE Acquisition

ICE, as a new exchange and relatively unknown outside the US, benefits from the global brand name of the NYSE. On its part, NYSE gains from ICE’s depth of experience in electronic trading. ‘It wasn’t until relatively late they [NYSE] joined the electronic trading scene -- NYSE can only benefit from the ICE experiences.’⁴⁵ NYSE Euronext hoped to revive sagging profitability by participating in ICE,⁴⁶ one of the most profitable companies in

³⁷ ‘ICE, NYSE Euronext Get HSR Nod for Merger’, *M&A Navigator* (online), 19 February 2013 <<https://global.factiva.com/>>.

³⁸ Aaron Lozada, ‘ICE/NYSE Euronext Deal Satisfies Regulatory Requirement as Antitrust Law Waiting Period Expires’, *SNL Specialty Finance M&A* (online), 1 March 2013 <<https://global.factiva.com/>>.

³⁹ ‘EU Clears, ICE, NYSE Euronext Stock Market Tie-up’, *Agence France Presse* (online), 24 June 2013 <<https://global.factiva.com/>>.

⁴⁰ Ibid; ‘European Commission Approves \$8.2 billion NYSE-Euronext Buyout by ICE’, *Associated Press Newswire* (online), 24 June 2013.

⁴¹ ‘SEC Approves NYSE Euronext Takeover by ICE’, *SeeNews Netherlands* (online), 19 August 2013 <<https://global.factiva.com/>>.

⁴² Ibid.

⁴³ ‘IntercontinentalExchange Expects to Close on NYSE Euronext Buyout on Nov 4’, *Associated Press Newswires* (online), 10 October 2013.

⁴⁴ ‘ICE NYSE Euronext Gets All Regulatory Approvals for Merger’, *Commodity Online* (online), 10 November 2013 <<https://global.factiva.com/>>.

⁴⁵ ‘ICE, NYSE Euronext Deal Opens Energy, Equity Synergy; More Control Over Agriculture’, above n 17.

⁴⁶ Michael J De La Merced, ‘Buffett Said to Have Weighed NYSE Euronext’, *The New York Times* (online), 29 January 2013 <<https://global.factiva.com/>>.

the industry despite its short history.⁴⁷ As an icon in the financial world, ICE declared that it would preserve the NYSE's physical presence in Lower Manhattan.⁴⁸

The NYSE-IntercontinentalExchange merger is expected to be a solid business combination. The alignment of derivative operations and clearing services acts as a strategic fit for both the companies. Alongside, the merger is expected to generate more than 15% of earnings accretion within the first year of completion of the deal. Going ahead, management projects run-rate expenses synergies of about \$450 million, which will be reaped in the second year of the merger startup. NYSE itself has generated \$82 million in cost savings so far in 2012 from its expense management plan that should produce cost synergies worth \$250 million, 33% of which is projected to be earned by the end of 2014.

Additionally, the merger will bring forth a strong competitive advantage by creating an end-to-end multi-asset portfolio and diversifying across the globe, while also vigorously tapping new opportunities in the emerging economies. Further, NYSE Liffe's both trading and clearing operations will be merged into ICE Clear Europe. This will create an excellent clearing model that is expected to grow by leaps once the interest rate volatility dissipates and interest rate swap clearing develops. The operational and capital efficiencies attained in both the U.S. and Europe will make the merged entity a dominant global player and well-positioned to take away the market share from leading derivative giant, CME Group Inc.

Hence, the merger is backed by a strong operating and competitive leverage, which will help the merged parties to generate enhanced operating cash flow, trading volumes and expense control. These factors will further aid IntercontinentalExchange to initiate annual dividends of about \$300 million, which is impressive given the current volatility, thereby amplifying the shareholders' value.

...

However, this is not the first time that NYSE is up for a merger. In February this year [2012], NYSE was compelled to terminate its \$10 billion merger with Frankfurt-based Deutsche Boerse due to the rejection from the regulators based on anti-trust concerns that were anticipated to create unhealthy competition. For similar regulatory, political and commercial hurdles, the take-over bid of \$11.3 billion, initiated together by IntercontinentalExchange and NASDAQ OMX Group Inc. (Nasdaq:NDAQ), got scrapped last year. At that time, IntercontinentalExchange was expected to take over NYSE's European futures markets (Liffe, Liffe U.S.) and the over-the-counter clearing business (NYPC).⁴⁹

Despite all the positive spin given to it, the deal involved significant execution risk and ICE was arguably paying a hefty premium.⁵⁰ The deal would also reduce 'the percentage of income ICE derives from its fast-growing derivatives business and add slow-growth businesses such as listings and market data services'.⁵¹ Cost savings produced by synergies, estimated at \$450 million of which 80% were to be realised by 2014, appeared overly

⁴⁷ Ibid.

⁴⁸ Ibid.

⁴⁹ 'The Zacks Analyst Blog Highlights: IntercontinentalExchange, NYSE Euronext, Morgan Stanley, CME Group and NASDAQ OMX Group', above n 23.

⁵⁰ Poelhuis, above n 16.

⁵¹ Ibid.

optimistic. A drop in ICE's P/E (price-to-equity) ratio, an important indicator, was predicted.⁵²

V POST-MERGER

ICE is now an industry powerhouse, with a combined market capitalisation of \$23 billion, operating 16 global exchanges and five central clearing houses.⁵³ ICE Chairman and CEO Jeffrey C Sprecher confidently touted the benefits produced by the merger:

This is a game changing transaction...

ICE now leads in terms of the breadth and depth of services, best-in-class technology, and access to markets and capital. We have significant opportunities ahead both to grow and to make the business more efficient and competitive. Our team will continue to keep our customers front and center on everything we do, while bringing new products to market in real time. We look forward to unlocking value together both for customers and shareholders.⁵⁴

For a chastened NYSE, the acquisition was yet another structural change and one undertaken in the interests of improving competitiveness, by creating a more diversified business model. In a joint statement, ICE President and NYSE Group CEO Duncan L. Niederauer, stated, 'This is a great strategic fit for both companies. We now have a stronger and more diversified business model, which leverages the iconic NYSE Euronext brand, our leadership in listings, equity options and interest rate markets with ICE's attractive portfolio of markets, clearing houses and technology for the global derivatives markets'.⁵⁵

A Relieving the Pressure for Regulatory Change

One of the reasons NYSE Euronext did not achieve the cost savings benefit that was anticipated prior to the merger can be attributed regulatory impediments on the US side. ICE, however, wanted to disengage from the EU almost immediately after its acquisition of NYSE Euronext; interjurisdictional regulatory concerns were thus not as problematic. It will take another merger involving a US exchange and an EU exchange to bring the regulatory issues to the fore again.

⁵² Adam Cancryn, 'Cost Savings Projections for ICE/NYSE Euronext Deal Too Optimistic, Credit Agricole Says', *SNL Energy Finance Daily* (online), 24 December 2012 <<https://global.factiva.com/>>.

⁵³ 'IntercontinentalExchange Completes Acquisition of NYSE Euronext', *PR Newswire* (online), 13 November 2013 <<https://global.factiva.com/>>.

⁵⁴ Ibid.

⁵⁵ Ibid.

A.4 EURONEXT AFTER THE BIG DEAL^{*}

I THE SALE

In December 2012, Intercontinental Group, (ICE) a major US derivatives exchange operator, revealed its intention to buy NYSE-Euronext, Inc. Approved by the European regulator in November 2013, the marriage was not made in heaven. A few months later, in June 2014, the ICE Group further announced its intention to sell the European component of NYSE – Euronext in an 845 million euro (\$1.2 billion) initial public offering of 4.2 million shares.

Euronext would be established as a stand-alone, publicly traded company.¹ With the dismemberment of NYSE-Euronext, the dream of a transatlantic trading venue ended, and with it, the grandiose expectations that the 2008 merger had engendered. Against the backdrop of exchange consolidations around the world, what is the significance of the failure of NYSE-Euronext? Is it the exception, or will it prove the rule?

The dismantling of NYSE-Euronext reflected the desire of ICE to focus on derivative products, on the one hand, and its retrenchment to the Anglo-American market, on the other. It came as no surprise that the purchase of the entire NYSE-Euronext group was merely a first step for ICE in obtaining LIFFE, the London derivatives platform which was the real prize.² Jeff Specher, the Chief Executive of ICE, had already shown a marked interest in expanding his reach in the derivatives markets.³

Derivatives trading is a profitable activity compared to low-margin equities trading, where profits have been eroded by the rise of alternative trading systems in recent years.⁴ In particular, derivative trading and clearing at LIFFE had been the most profitable and fastest growing part of Euronext; in the preceding decade, trading listed derivatives had grown by 14 percent annually.⁵

As early as December 2012, observers had noted the disinterest of ICE on the European side of the transaction. Europe ‘has never been part of (ICE) empire’.⁶ Emissions and commodity trading were its forte, not equities, so apart from the crown jewel of LIFFE, there was not much interest in Euronext’s other activities.⁷ Derivatives had been the motor of growth for Euronext.⁸

^{*} The author would like to acknowledge, in particular, the assistance of Adrien Faelli with this chapter.

¹ Chad Bray, ‘Intercontinental Exchange Set to Spin Off Euronext’, *The New York Times* (online), 27 May 2014 <http://dealbook.nytimes.com/2014/05/27/intercontinentalexchange-announces-plans-to-float-euronext/?_r=0>.

² Philip Stafford, ‘Quick View: ICE’s Zest for Liffe’, *Financial Times* (online), 20 December 2012 <<http://www.ft.com/cms/s/0/f4a1fc88-4a88-11e2-968a-00144feab49a.html>>; Jacob Bunge ‘SEC Approves ICE-NYSE Deal’, *Wall Street Journal* (online), 16 August 2013 <<http://www.wsj.com/articles/SB10001424127887323639704579016521606693810>>.

³ Namely, the London Metal Exchange that he tried to acquire.

⁴ Especially newly entrants MTFs, see below, chapter II.

⁵ Philip Stafford, ‘Euronext Prepares to Relist for “a New Era”’, *Financial Times* (online), 2 June 2014 <<http://www.ft.com/cms/s/0/75d8ff52-e62f-11e3-bbf5-00144feabdc0.html>>; see also World Federation of Exchange, *WFE Database* <<http://www.world-exchanges.org/statistics>>.

⁶ Stafford, ‘Quick View: ICE’s Zest for Liffe’, above n 2.

⁷ Ibid.

⁸ Stafford, ‘Euronext Prepares to Relist for “a New Era”’, above n 5.

As of June 2014, Euronext floated free. In Europe's highly fragmented equities market, Euronext has been pitched into a charged, competitive game. Some see opportunities though to reformulate finance and its regulation in a truly European mode and casting off the dominant Anglo-American model.⁹

II THE NEW EURONEXT

A Toward a Refocus on Post-Crisis European Finance

Until the initial public offering in June 2014, Euronext had never taken the form of a publicly traded company.¹⁰ Not surprisingly, the prospectus, a selling document after all, emphasises the European dimension of its future operations. Euronext's ambition is to reposition itself as a European centre for capital raising by building a pan-European exchange group active in several countries and in a wide range of European products.¹¹ Euronext is already a leader in European cash equities, but plans to expand into exchange traded funds, corporate bonds (including Eurobonds, now mainly traded on the Luxembourg Stock Exchange), and, despite the loss of LIFFE, continue developing the derivatives and commodity markets.¹²

In its initial public offering, Euronext also insists on the competitive advantages of European integration which provides a harmonized regulatory framework, single technology and a federal structure to the market.¹³ Even the global financial crisis gets a positive spin, as having revealed Europe's macroeconomic position.¹⁴ After the 2008 crisis and the volatility that followed, Euronext hopes to ride the recovery in the European cash equities market amid predictions of growth by the European Commission.¹⁵ Euronext also added EnterNext to its stable, a trading venue for small and medium sized enterprises which has experienced significant growth since its creation in 2013. EnterNext offers a pan Europe alternative to capital raising, while benefiting from Euronext's regulatory framework and transparency.¹⁶

The new shareholder base, primarily large European institutional investors, reflects the new European focus.¹⁷ Inevitably, there is the political dimension; European institutional investors indicating to international markets that they are prepared to support their own.¹⁸ Also, the latest EU legislative initiatives, such as MiFID II, will reshape the financial regulatory landscape.¹⁹ Heightened competition among different trading venues, pressures regulated

⁹ Aurélien Broncard, 'Introduction en bourse d'Euronext, pour une bourse paneuropéenne (enfin) compétitive', *les échos* (online), 12 June 2014, <<http://www.lesechos.fr/idees-debats/cercle/cercle-99979-introduction-en-bourse-deuronext-pour-une-bourse-paneuropeenne-enfin-competitive-1012141.php?EykcxzPRwzYfyg1D.99>>.

¹⁰ Euronext N.V., *Prospectus* (10 June 2014) 6 <<https://www.euronext.com/en/ipo>>.

¹¹ Ibid 110, 114.

¹² Ibid 114.

¹³ Ibid 112.

¹⁴ Ibid 71.

¹⁵ Ibid; Euronext, *2014 Annual Review* (February 2015) <<https://www.euronext.com/fr/about-euronext>>.

¹⁶ Ibid; Enternext, 'Euronext Announces Monthly Trading Volumes for May 2015' (Press Release, 3 June 2015) <<https://www.enternext.biz/en/news/euronext-announces-monthly-trading-volumes-may-2015>>.

¹⁷ Such as ABN Amro Group NV and BNP Paribas SA, Banco Espírito Santo, Euroclear and Société Générale.

¹⁸ Broncard, above n 9.

¹⁹ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on Markets in Financial Instruments and Amending Directive 2002/92/EC and Directive 2011/61/EU [2003] OJ L 173/349 ('Directive on Markets in Financial Instruments (Mifid II)').

markets such as Euronext to innovate with new product development, creating a virtuous circle of opportunity for European financial institution.²⁰

B 'Everything Old is New Again'

The structure of the new Euronext N.V. has changed little from the old Euronext. The Paris, Brussels, Lisbon and Amsterdam exchanges are still a part of Euronext. Euronext is still listed in Amsterdam which is also host to SmartPool, Euronext's pan-European dark pool. A major loss is LIFFE, the London based futures exchange, which ICE has retained. Nevertheless, putting a brave face on affairs, Euronext has developed other platforms as it adapts to its new-found independence. EnterNext is one such initiative, providing an alternative to traditional bank funding which has proved increasingly harder to obtain. EnterNext also provides the advantages of a regulated market.²¹ AlterNext, is another such initiative, a Euronext multilateral trading platform.

EnterNext has done particularly well, a long-term project of Euronext predating the breakup by ICE. A year after its creation in 2013, EnterNext reached 9 billion Euros in capital raised.²² In June 2014, EnterNext added to its services by launching two programmes designed to improve quantitative equity research and rating and give more visibility to its listed equities.²³

Despite the loss of LIFFE, Euronext still operates a subsidiary in London, Euronext UK Markets, which, in June 2014, was granted the status of UK Recognized Investment Exchange, in accordance with the *Financial Services and Markets Act 2000*. Euronext UK Markets aims to attract international issuers looking to list in London while enjoying access to Euronext other markets.²⁴ By listing in London, securities are traded on Euronext's UTP that connects all its European securities markets, representing Europe's largest cross-border equity exchanges. In this way, Euronext seeks to improve its visibility at the international level.

Post trade services have also been slightly modified. Euronext no longer owns a clearinghouse and uses the London Stock Exchange Group-controlled LCH.Clearnet to clear its cash and derivatives trades.²⁵ Euronext will enjoy a continuous stream of income due to a revenue sharing agreement with LCH.Clearnet.²⁶ However, the arrangement does make

²⁰ Broncard, above n 9.

²¹ Euronext, *Propectus*, above n 10, 120.

²² Enternext, *One Year On, SME Financing Facilitator EnterNext Is on Track to Meet Targets* (10 July 2014) <https://www.enternext.biz/en/news/one-year-sme-financing-facilitator-enternext-track-meet-targets#_ftn1>.

²³ By entering into an agreement with Morningstar, a provider of investment research: Enternext, *EnterNext Boosts SME Equity Research and Supports Technology Sector with Two Initiatives* (2 June 2014) <<https://www.enternext.biz/en/news/enternext-boosts-sme-equity-research-and-supports-technology-sector-two-initiatives>>.

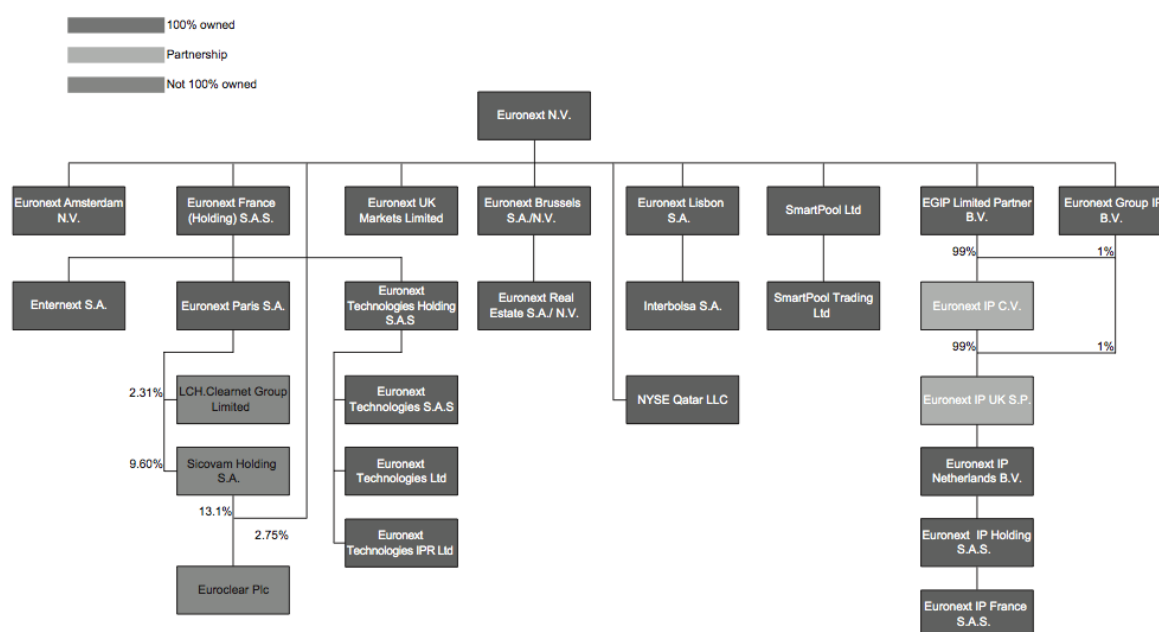
²⁴ New York Stock Exchange, 'Euronext UK Markets Limited receives FCA approval for RIE status' (News Release, 4 June 2014) <<http://www1.nyse.com/press/1401280737728.html>>

²⁵ Euronext, *2014 Annual Review*, above n 15.

²⁶ Which constituted 8% of its revenues in 2014: Euronext, *Prospectus*, above n 10, 6.

Euronext dependent on a rival, so it is not inconceivable that Euronext may seek to gain greater control of its clearing operations.²⁷

Figure 1 Structure of Euronext N.V. as of June 2014²⁸



C Activities

Euronext's main activities continue to be listing, cash trading, derivatives trading and commercialisation of market data, post-trade and market solutions. As of March 2014, Euronext placed second among the largest European exchange groups in terms of market capitalisation of listed companies and number of companies listed, and third in terms of open interests of derivatives traded.²⁹

In 2014, equity trading and data constituted the main sources of revenue for Euronext, while derivatives still accounted for only 10 percent of the group turnover. With cash equities remaining the core business of Euronext, margins have eroded during the last decade due to the emergence of multilateral trading facilities.³⁰

Euronext is now seeking to diversify its activities, especially in terms of derivatives, which was once its most profitable activity.³¹ Euronext CEO expressly stated the intention to 'inject significant innovation and ... relaunch derivatives contracts for Euronext on the continent', in

²⁷ Philip Stafford, 'Long-Term Questions as Euronext's Momentum Gathers Pace', *Financial Times* (online), 22 December 2014 <<http://www.ft.com/cms/s/0/c80e83d8-876e-11e4-8c91-00144feabdc0.html>>.

²⁸ Euronext, *Propectus*, above n 10, 218.

²⁹ Ibid 110.

³⁰ Josanco Floreani and Maurizio Polato, *The Economics of the Global Stock Exchange Industry* (Palgrave Macmillan, 2013) 62; Philip Stafford, 'Euronext Valued at Up To €1.75bn in Flotation', *Financial Times* (online), 10 June 2014 <<http://www.ft.com/cms/s/0/0cb9ba2e-efcc-11e3-bee7-00144feabdc0.html>>.

³¹ Stafford, 'Euronext Prepares to Relist for "a New Era"', above n 5; Stafford, 'Long-Term Questions as Euronext's Momentum Gathers Pace', above n 27.

order to reduce reliance on equities.³² As part of its diversification strategy, Euronext is licensing indices to financial institutions to create its own products, and expanding over-the-counter trade services.³³ Additionally, making use of its links to European agriculture, Euronext has sought to develop new commodity futures, such as the milling wheat futures contracts, and rapeseed oil futures, in the biodiesel sector.³⁴ Overall, in 2014, Euronext has launched 279 new products across its derivatives and commodities business.³⁵

Apart from equity and derivatives trading, Euronext receives most of its revenues from listing; there are 1300 issuers listed with a combined market capitalisation of over €2.8tm in 2014.³⁶ Euronext is also active in the market data business and licensing of products on Euronext indices, which constituted, in 2014, 20% of its revenue.³⁷ Lastly, market solutions and services to exchanges are still one of the core businesses of Euronext, which has developed electronic trading platforms, such as the Universal Trading Platform (UTP), previously developed by NYSE Euronext. UTP is currently still the property of ICE, which has licenced it to Euronext (through Euronext IP CV) on a permanent, non-revocable and royalty-free basis.³⁸

Apart from the loss of the important derivative trading business, Euronext's activities on its home continent remain mostly unchanged. But the worry remains that the equity market alone might not be sufficient to weather the next, inevitable, European financial crisis. Euronext has thus embarked on the difficult task of building a new derivatives business to replace the one it lost in LIFFE.

III PERSPECTIVE: EURONEXT AND THE TREND TOWARD CONSOLIDATION OF STOCK EXCHANGES

At first glance, the break-up of NYSE-Euronext appears an anomaly, running counter to the pronounced trend towards stock exchange consolidation and integration. Indeed, during the last decade, several major markets merged into bigger, transcontinental entities.³⁹ The usual suspects, globalization, deregulation, and technological development, broke down the barriers.⁴⁰ Consolidation is attractive, as it may produce long-term benefits for investors and institutions due to international diversification of products.⁴¹ In 2007, the CEO of NYSE – Euronext confidently predicted only three major financial markets in the future.⁴²

Thinking has changed however. Euronext's failed merger with Deutsche Börse marks the shift. The European commission, in February 2012, expressed its opposition to this merger as

³² Stafford, 'Long-Term Questions as Euronext's Momentum Gathers Pace', above n 27.

³³ Ibid.

³⁴ Euronext, *Prospectus*, above n 10; Euronext, *2014 Annual Review*, above n 15.

³⁵ Euronext, *2014 Annual Review*, above n 15.

³⁶ Ibid.

³⁷ Ibid.

³⁸ Euronext, *Prospectus*, above n 10, 169.

³⁹ Euronext and NYSE in 2007, NASDAQ and OMX in 2008, London Stock Exchange and Borsa Italiana in 2007, ISE and Deutsche Borse in 2007.

⁴⁰ Ekaterina Dorodnykh, *Stock Market Integration: An International Perspective* (Palgrave Macmillan, 2013) 7; see also Frederic S Mishkin, *The Economics of Money, Banking, and Financial Markets* (Pearson Addison Wesley, 2007).

⁴¹ Dorodnykh, above n 40, 9; Floreani and Polato, above n 30, 37.

⁴² Annick Masounave, 'NYSE Euronext: un groupe diversifié et innovant' (2008) 400 *Revue Banque* 41.

‘it would have resulted in a quasi-monopoly in the area of European financial derivatives traded globally on exchanges’, with 90% of the European markets controlled by the same entity.⁴³ European competition law proved the first hurdle slowing the rush towards consolidation.

Additionally, some began to question the merger model, dominant for the last decade, in terms of adding value for shareholders. Should markets be smarter rather than bigger?⁴⁴ A battle for redistribution of the ownership of key assets, such as LIFFE or LCH.Clearnet, might be the next wave.⁴⁵ The failure of NYSE-Euronext highlights a different trend; investors are looking for certain specific strategic assets and regulators are less likely to allow mega-mergers to proceed.⁴⁶

For Euronext, the challenge is to compensate for the loss of LIFFE, the London derivatives market which was its crown jewel. After June 2014, Euronext multiplied its efforts to extend activities to other more promising areas, including the development of new products such as futures and commodities that took an important part in the promotion of the venue⁴⁷. ICE dropped Euronext and its equities business but kept LIFFE and the derivatives business for good reason. Slowdowns in the equity markets of recent years and fierce competition from alternative trading venues have only made matters worse for Euronext.⁴⁸

Responsibility for this enhanced competition is partly due to evolving European regulation. With the adoption of MIFID in 2007, the European Union introduced multilateral trading platforms (MTFs), with a view to promoting more competition in the equity markets, due to MTFs lower transaction costs, reduced bid-ask spreads and faster trading times.⁴⁹ The increased number of trading venues has also caused fragmentation of the markets and a growth in ‘dark-trading’ off market.⁵⁰ Overall, Euronext, once the first transatlantic exchange,⁵¹ now competes with other pan-European markets, be they regulated or alternative venues, such as Bats Chi-X Europe, the London Stock Exchange and Deutsche Börse.

Since its initial public offering, Euronext has been scrambling. The group has massively launched itself into derivative products. In 2014, Euronext introduced more than 270 new

⁴³ European Commission, ‘Mergers: Commission Blocks Proposed Merger between Deutsche Börse and NYSE Euronext’ (Press Release, 1 February 2012) <http://europa.eu/rapid/press-release_IP-12-94_en.htm>.

⁴⁴ Stafford, ‘Quick View: ICE’s Zest for Liffe’, above n 2.

⁴⁵ Stafford, ‘Euronext Prepares to Relist for “a New Era”’, above n 5; see also Floreani and Polato, above n 30, 38; the authors mention the case of LSEG and LCH.clearnet.

⁴⁶ Such as the failed 2012 Deutsche Borse and Euronext merger, see European Commission, ‘European Commission Blocks Proposed Merger between Deutsche Boerse and NYSE Euronext’, above n 43; Philip Stafford, Arash Massoudi and Jeremy Grant, ‘ICE and NYSE Euronext Go Where Other Exchanges Have Struggled’, *Financial Times* (online), 3 October 2013 <<http://www.ft.com/cms/s/0/c6c899fc-2b56-11e3-bfe2-00144feab7de.html>>; Martin Waller, ‘Talks to Create World’s Biggest Exchange’, *The Times* (online), 8 December 2008 <<http://www.thetimes.co.uk/tto/business/industries/banking/article2159728.ece>>.

⁴⁷ Stafford, ‘Quick View: ICE’s Zest for Liffe’, above n 2.

⁴⁸ Committee of European Securities Regulators (CESR), ‘Impact of MiFID on Equity Secondary Markets Functioning’ (Report No 09/355, European Securities and Markets Authority, 10 June 2009) 10 (‘2009 CESR Equity Market Report’) <http://www.esma.europa.eu/system/files/09_355.PDF>.

⁴⁹ European Commission, Directorate General Internal Market and Services, ‘Review of the Market in Financial Instruments Directive’ (Public Consultation, European Commission, 8 December 2010) (‘Consultation on the Review of MiFID’) <http://ec.europa.eu/internal_market/consultations/docs/2010/mifid/consultation_paper_en.pdf>.

⁵⁰ 2009 CESR Equity Market Report, above n 48.

⁵¹ ‘NYSE Group and Euronext Announce Merger’ (News Briefs, June 2006) <<http://www1.nyse.com/about/publication/1145959806931.html>>.

products in its quest to retrieve its derivatives market.⁵² At the same time, restructurings and job cuts were announced in order.⁵³ Fierce competition continues with BATS Chi-X and OTC services; revenues on activities such as trading and listing are in jeopardy. The share of trading in Euronext-listed securities has declined; technological adaptation is seen as the key to successful competition.⁵⁴

Potential political risk cannot be ignored. Massive changes in EU regulation might impair Euronext's ability to compete internationally⁵⁵. Rising populist sentiments in Europe might also jeopardize the future of a pan-European financial initiative known as the capital markets union.⁵⁶

On the other hand, fears about the viability of an independent Euronext appear to be laid to rest.⁵⁷ Vulnerability to takeover by a foreign group was the issue.⁵⁸ In the event, these fears dissipated, as several major European institutions became keystone investors in the course of the share offering engineered by ICE.

Years of pressure from the rising prominence of competing MTFs, though has been offset by kinder regulatory action from the European Union in the run up to the adoption of MiFID II.⁵⁹ The latter, as well as European Market Infrastructure Regulation (EMIR), purportedly favour on-exchange trading thus providing renewed impetus and growth opportunities for exchanges.⁶⁰ In particular, MiFID II assigns a particular importance to transparency and publicity requirements, which will be extended beyond stock exchanges, also affecting OTC operations. The preamble to MiFID II makes this explicit:

‘The evolution of financial markets has exposed the need to strengthen the framework for the regulation of markets in financial instruments, including where trading in such markets takes place over-the-counter (OTC), in order to increase transparency, better protect investors, reinforce confidence, address unregulated areas, and ensure that supervisors are granted adequate powers to fulfil their tasks’.⁶¹

It is expected that MiFID II will contribute to bringing a large part of financial operations onto regulated venues, especially ETFs.⁶² Euronext stands to gain from this movement to public exchanges, yet concerns remain as to the “level playing field”. New trading platforms

⁵² Euronext, *2014 Annual Review*, above n 15, 11.

⁵³ Stafford, ‘Euronext Prepares to Relist for “a New Era”’, above n 5.

⁵⁴ Euronext, *Prospectus*, above n 10, 29–33.

⁵⁵ *Ibid.*

⁵⁶ Stafford, ‘Euronext Prepares to Relist for “a New Era”’, above n 5.

⁵⁷ ‘Euronext: on ne meurt que deux fois’, *Le Monde* (online), 6 April 2013 <<http://lauer.blog.lemonde.fr/2013/04/06/euronext-on-ne-meurt-que-deux-fois>>.

⁵⁸ Tim Cave and Michelle Price, ‘Euronext Weighs Postdeal Plans’, *Wall Street Journal* (online), 13 May 2013 <<http://www.wsj.com/articles/SB10001424127887323716304578481280506585300>>.

⁵⁹ Euronext, *2014 Annual Review*, above n 15.

⁶⁰ *Ibid.*

⁶¹ *Directive on Markets in Financial Instruments (Mifid II)* [2003] OJ L 173/349.

⁶² Euronext, *Prospectus*, above n 10, 104. ‘On-exchange ETFs in Europe are expected to see further growth for the following reasons. In Europe, OTC-executed ETFs are estimated to account for a large majority of the overall volume. Hence the trading value of ETFs on exchanges reflects only a small portion of the overall market activity. MiFID II is expected to drive much of the activity into regulated venues, i.e., exchanges’.

are on the horizon, especially the Organised Trading Facilities (OTFs), which would exist alongside MTFs and regulated markets such as Euronext.⁶³

In the interim though, results for 2015 show Euronext's continued reliance on the equity markets, with only gradual development of its derivatives activity. Monthly trading volumes for March 2015 indicate a sharp increase in the average daily trading value in equities, together with growth of revenues from listings, but at the same time a drop in derivatives and commodity markets activities.⁶⁴

The dream of Euronext's founder, Jean-François Theodore, was to see Euronext as part of a transatlantic market or at least a unified continental trading venue.⁶⁵ Since the breakup of NYSE-Euronext in June 2014, a resurgence of interest in a new European trading venue and the relatively good 2015 results, have given hope to Euronext of restored fortunes. Yet the current focus on European finance smacks of resignation, in comparison to the optimism that prevailed during the NYSE – Euronext years. Euronext's current situation may mark a worldwide shift toward greater interest in regional, rather than global, markets; on the other hand, it may only represent Euronext's frustrated ambitions.

IV COMPETITION AND MiFID: HOW MTFs HAVE ERODED THE ACTIVITY OF TRADITIONAL VENUES

Fuelled by advances in technology, alternative trading systems have transformed landscape of capital markets in Europe. Alternative trading-systems, which are not regulated as stock exchanges, operate outside of traditional market hours, are faster and cheaper, and consequently contribute to creating a more competitive environment and to putting other venues under mounting pressures.⁶⁶

In 2006, the European Commission adopted the Markets in Financial Instruments Directive (MiFID, now usually referred to as MiFID I) to enhance competition and encompass the full range of investor-oriented activities in a single harmonised framework. MiFID I sought to establish 'transparent and non-discretionary rules and procedures that provide for fair and orderly trading', and to recognise 'the emergence of a new generation of organised trading systems alongside regulated markets'.⁶⁷ The efficient functioning and the integrity of the market necessitated regulatory oversight.⁶⁸

⁶³ NYSE Euronext, *Questionnaire on MiFID/MiFIR 2: Review of the Markets in Financial Instruments Directive* (22 February 2012) European Parliament <<http://www.europarl.europa.eu/document/activities/cont/201202/20120222ATT38994/20120222ATT38994EN.pdf>>.

⁶⁴ Euronext, 'Euronext Announces Monthly Trading Volumes for March 2015' (Press Release, 3 June 2015) <<https://www.euronext.com/en/news/euronext-announces-monthly-trading-volumes-march-2015>>.

⁶⁵ Michael Stothard and Philip Stafford, 'Jean-François Théodore, Architect of Euronext, 1946-2015', *The Financial Times* (online), 20 May 2015 <<http://www.ft.com/cms/s/0/1201819a-fe41-11e4-be9f-00144feabdc0.html>>.

⁶⁶ Dorodnykh, above n 40, 19; see also Gianni Nicolini, *L'integrazione dell'exchange industry europea* (Università di Roma Tor Vergata, 2010); as to the elements calling for recognition by legislators, see Peter Gomber and Markus Gsell, 'Catching Up with Technology – The Impact of Regulatory Changes on ECNs/MTFs and the Trading Venue Landscape in Europe' (2006) 1(4) *Competition and Regulation in Network Industries* 535.

⁶⁷ *Directive on Markets in Financial Instruments (Mifid II)* [2003] OJ L 173/349, whereas (5).

⁶⁸ *Ibid.*

Since they perform the same functions of providing organised trading venues, MiFID I aligns the definitions of MTF and Regulated Market (ie an exchange such as Euronext);⁶⁹ however, they are not subject to the same regulatory requirements. For example, rules regarding organisational requirements under articles 13, 14, and 39 are more demanding for Regulated Markets than for MTFs. Also, disclosure and transparency requirements are higher for Regulated Markets, and trading on Regulated Markets subject to stricter rules than on non-regulated markets.⁷⁰ The justification for the differences resides in the predominance of equity trading in the Regulated Markets, among other factors.⁷¹

MiFID I was supposed to increase competition in the market place by allowing new actors with better technological abilities to enter.⁷² For the same reason, MiFID I discouraged concentration of trading and consolidation, as previously permitted by the Investment Services Directive, which left member states free to support a single trading venue⁷³. As a consequence, traditional venues experienced an unprecedented retrenchment.⁷⁴

With the appearance of MTFs, European stock exchanges began to lose market share. As an example, according to Gomber and Pierron (2010), primary exchanges still enjoyed a 100 percent market share in Eurostoxx 50 at the beginning of the year 2008, but their share fell abruptly to 78 percent by the end of 2009.⁷⁵ According to other sources, MTFs represented less than 6% of total European market share in 2008, but 26% in 2011.⁷⁶ Undisputedly, alternative trading venues have known a dramatic increase since 2008, to the detriment of stock exchanges.

In its report on the effects of MiFID I on European secondary markets in 2009, the EU reached the same conclusion: MTFs have drained liquidity away from the regulated markets and OTC spaces, even though other causes, such as volatility may be at work.⁷⁷ MTFs offer more opportunities for pan-European trading because of their broader range.⁷⁸ However, at the time, the EU report stated ‘the majority of trading remains on the incumbent regulated markets rather than new entrants and OTC’.⁷⁹ This state of affairs has substantially evolved since 2009.

Stock exchanges reacted in different ways to increased competition from MTFs, beginning with structural changes. To decrease their costs, increase their market share and maintain liquidity, stock exchanges merged; they entered into alliances which resulted in groups active

⁶⁹ Ibid.

⁷⁰ Euronext, *Prospectus*, above n 10, 100.

⁷¹ ‘2009 CESR Equity Market Report’, above n 48, 31.

⁷² ‘Consultation on the Review of MiFID’, above n 49, 5.

⁷³ Floreani and Polato, above n 30, 76: the authors compare MiFID with the U.S. regulation NMS, also designed to improve competitive policies; see also ‘2009 CESR Equity Market Report’, above n 48, 8.

⁷⁴ This point has already attracted a lot of academic attention, see Peter Gomber and Axel Pierron, ‘MiFID - Spirit and Reality of a European Financial Markets Directive’ (September 2010), <SSRN: <http://ssrn.com/abstract=1858605>>; Nicolini, above n 66; Tanja Boskovic, Caroline Cerruti, and Michel Noel, ‘Comparing European and U.S. Securities Regulations’ (Working Papers No 184, World Bank, 2010).

⁷⁵ Gomber and Pierron, above n 74.

⁷⁶ FESE statistics, Federation of European Securities Exchanges, <www.fese.eu>

⁷⁷ ‘2009 CESR Equity Market Report’, above n 48, 5.

⁷⁸ Ibid.

⁷⁹ Ibid 35.

on an international scale with a wider range of products⁸⁰. Euronext and NYSE in 2007 was the poster child, but NASDAQ and OMX, the London Stock Exchange and Borsa Italiana, and ISE and Deutsche Börse also represent the trend. Integration and consolidation were not entirely new phenomena; globalisation and deregulation were also factors pushing in that direction.⁸¹

As a defensive measure, established exchanges started to create their own MTFs, in the hope of recapturing market share that had drifted away to independent platforms.⁸² Euronext launched its dark pool trading platform (SmartPool) for large transactions in February 2009.

Exchanges also complained about organisational requirements that could result in a lighter regulatory load for MTFs despite similarities in nature and size⁸³. Equally problematic were uncoordinated trade monitoring requirements even where the same financial instruments were traded on different platforms.⁸⁴

MiFID I also provide waivers for pre-trade transparency requirements.⁸⁵ A firm operating a trading system has an obligation to disclose the five best price levels for both bids and offers for each security, including the number of shares and orders.⁸⁶ However, MiFID I also provides for certain waivers, which permit the creation of dark pools.⁸⁷ Still, disclosure requirements and pre-trade transparency have a certain importance for the price discovery process and the efficient functioning of the market⁸⁸. Thus, exchanges noted that trading moving away to OTC platforms or dark pools, not subject to these requirements, “might raise price formation issues and lightly supervised platforms create systemic risk to the market.”⁸⁹

With the arrival of subsequent EU directives, notably MiFID II, Euronext has continued to push for harmonisation of the pre-trade transparency requirements for all trading venues, as well as for harmonised waivers to ensure a level playing field.⁹⁰ The retrenchment in OTC spaces and the extension of the transparency requirements may bode well for the traditional exchanges.

⁸⁰ Ibid 63; Floreani and Polato, above n 30.

⁸¹ Dorodnykh, above n 40; Cheol Eun and Jinsoo Lee, ‘Mean-variance Convergence Around the World’ (2010) 34 *Journal of Banking & Finance* 856; Frederic Mishkin, ‘Is Financial Globalization Beneficial?’ (2007) 39 *Journal of Money, Credit and Banking* 259.

⁸² ‘2009 CESR Equity Market Report’, above n 48, 10; A concurrent phenomenon is the creation of other forms of MTFs to capture specific categories of issuers that did not fulfill the conditions to emit on regulated markets, like Euronext’s MTF, Alternext, a special venue for SME.

⁸³ ‘Consultation on the Review of MiFID’, above n 49, 18.

⁸⁴ Ibid.

⁸⁵ Committee of European Securities Regulators, ‘Waivers from Pre-trade Transparency Obligations under the Markets in Financial Instruments Directive (MiFID)’ (Report, European Securities and Markets Authority, 20 May 2009) <http://www.esma.europa.eu/system/files/09_324_Update_22102010.pdf>.

⁸⁶ Erik Banks, *Dark Pools: The Structure and Future of Off-Exchange Trading and Liquidity* (Palgrave MacMillan, 2010) 13.

⁸⁷ Ibid.

⁸⁸ ‘2009 CESR Equity Market Report’, above n 48, 25.

⁸⁹ Ibid.

⁹⁰ NYSE Euronext, *Questionnaire on MiFID/MiFIR 2: Review of the Markets in Financial Instruments Directive*, above n 63, 15–17.

Two warring factions now compete at each point of the exchange industry's value chain, large coalitions of exchanges which have resulted from mergers and flexible MTFs, which now make up an important part of the market.⁹¹

In 2009, the EU had concluded that the majority of trading took place on Regulated Markets, not on MTFs. By 2015, this was no longer the case. One MTF is now the single largest trading venue in Europe. The assumptions supporting regulatory differentiation between the Regulated Markets and MTFs no longer hold.⁹²

V CHI-X: A FIRST IN EUROPE

MTFs have dramatically grown in importance in Europe since they began to appear in 2007. They have drained liquidity from the traditional exchanges to the point where they now dominate the trading markets in Europe.

Chi-X and BATS Europe began as two separate pan-European MTFs but merged in 2011 to form BATS Chi-X Europe, which, in terms of market share and trading value, is Europe's largest equity exchange. This consolidated group of MTFs represents a quarter of the entire European equities trading market.⁹³

In 2013, BATS Chi-X Europe attained the status of Recognized Investment Exchange (RIE) from the London Financial Conduct Authority (FCA), its regulator. BATS Chi-X Europe can now compete head on with traditional exchanges for primary listing and derivatives contracts. Importantly, RIE status provides greater access to retail investors; some brokers must act exclusively through formal exchanges under the terms of their mandates.⁹⁴ An RIE can operate both MTFs and Regulated Markets (as defined in Articles 4.14 and 4.15 of MiFID I. Notably, BATS Chi-X Europe shares this status with Euronext's subsidiary, Euronext London Limited, which is also a RIE⁹⁵.

Although a relatively new trading platform, BATS Chi-X Europe quickly became a main competitor to Euronext, since RIE status combines the flexibility of MTF with the security and transparency offered by Regulated Markets, with superior technology and attractive prices. The competition however does not stop there. MiFID I also brought change to the European landscape of post-trade services, by allowing competition between clearing houses. New MTFs looked to make arrangements with newly established central counterparties (CCP) for their clearing and settlement activities.⁹⁶ BATS Chi-X Europe trades used to be conducted through and guaranteed by the European Multilateral Clearing Facility (EMCF,

⁹¹ Floreani and Polato, above n 30, 65.

⁹² The issue was already raised in 2010, see '2009 CESR Equity Market Report', above n 48, 25.

⁹³ Philip Stafford, 'UK Authorities Clear BATS Takeover of Chi-X', *Financial Times* (online), 24 November 2011 <<http://www.ft.com/intl/cms/s/0/5b5ce1cc-15f6-11e1-b4b1-00144feabdc0.html#axzz3dGlfxkqR>>.

⁹⁴ Philip Stafford, 'BATS Europe given UK exchange status' *Financial Times* (online), 9 May 2013 <<http://www.ft.com/intl/cms/s/0/29990036-b8bf-11e2-869f-00144feabdc0.html#axzz3dGlfxkqR>>.

⁹⁵ Bank of England, Prudential Regulation Authority, *Recognized Investments Exchanges*, Financial Conduct Authority <<https://www.fsa.gov.uk/register/exchanges.do>>.

⁹⁶ '2009 CESR Equity Market Report', above n 48, 21.

now ECCP). Now, by a process of interoperable clearing, participants can choose among three clearinghouses, including LCH.cleartnet.⁹⁷

MTFs and formal exchanges have had different operational strategies. Exchange consolidations prompted by competitive concerns did not seem to extend to MTFs. However, with the BATS Chi-X Europe merger the consolidation bug has hit MTFs, looking for the advantages associated with size. MTFs are also eyeing alliances with official stock exchanges, in pursuit of extended trading hours and greater visibility among investors.⁹⁸

Competition among trading venues in Europe continues to rage. At its inception, the market share of BATS Chi-X Europe stood close to a remarkable 25 percent of the European market; by 2014 it had dipped to just over 20 percent. BATS Chi-X Europe responded with tiered pricing in an effort to regain market share and remain the dominant European trading venue.⁹⁹ The strategy was successful, at least in the short term; by May 2015, BATS Chi-X Europe had regained market share, rising to 24.4 percent of the total European market,¹⁰⁰ ahead of both Euronext and the London Stock Exchange. With its emphasis on advanced trading technology, BATS Chi-X Europe has also attracted high frequency trading (HFT), becoming the favourite European venue for HFT.¹⁰¹

Since the adoption of MiFID I, traditional European exchanges have been facing ferocious competition from upstart MTFs. As new entrants, MTFs enjoy a technological advantage; in addition to their technical superiority, MTFs also offer a wider range of products. The formal exchanges have been pressured to upgrade and modernise their own trading platforms. Consolidation and the pursuit of a growth strategy through mergers to form larger groups, in a chase for volume and liquidity, continue apace. MTFs like BATS Chi-X Europe have also entered the merger game for the same reasons, as well as increasing competition for primary listings, formerly a preserve of the regulated exchanges. In this context of fragmentation and growing competition, the fate of Euronext as an independent European platform is still uncertain, unless deconsolidation becomes a general trend.

⁹⁷ *Clearing*, BATS Chi-X Europe <<http://www.batstrading.co.uk/clearing/>>.

⁹⁸ Nicolini, above n 66; let us also mention the MTF turquoise, which has been created by investment firms to compete with stock exchanges.

⁹⁹ Philip Stafford, 'BATS Chi-X Bids to Win Back Europe Market Share', *The Financial Times* (online), 3 April 2014 <<http://www.ft.com/intl/cms/s/0/8ed83cc4-bb38-11e3-b2b7-00144feabdc0.html>>.

¹⁰⁰ BATS, 'BATS Reports Continued Strong Market in May; Second-Best Month for U.S. Options Business, 21.2% U.S. Equities Market Share' (Press Release, May 2015) <http://cdn.batstrading.com/resources/press_releases/BGM_May2015_Volume_FINAL.pdf>; see also BATS, *Notional Value Summary* <http://www.batstrading.co.uk/market_data/market_share/index/>.

¹⁰¹ Antoine Bouveret et al, 'High-frequency Trading Activity in EU Equity Markets' (ESMA Economic Report No 1, European Securities and Markets Authority, 2014).

Part B London – Prey and Predator

B.1 LONDON – PLAYING HARD TO GET*

I INTRODUCTION

The new global financial landscape has seen one of the most iconic of financial institutions, the stock exchange, adapting to systemic change through demutualisation and forging relationships with other exchanges and pre or post-trade service providers across the globe. As these relationships developed and technology advanced, some exchanges sought to merge, creating enormous global trading platforms operating remotely across the world. Bourses sought to boost profit margins by diversifying their revenue streams through investments in post-trade services, the provision of information and creating platforms trading more sophisticated, modernised financial instruments.

Despite what its exclusive membership may have initially thought, the London Stock Exchange¹ was not immune to any of this. Its journey over the past 30 years commences, with the Big Bang of 1986. Like a magnet, this event attracted investment from the Continent and later, attention from other major exchanges and businesses around the world. In order to explore the LSE's interactions with other exchanges over the past 15 years of the 21st century it is necessary to understand the attitude of the LSE prior to and during deregulation, and the necessary shifts in attitude it had to make in light of the changes occurring across the Atlantic and throughout Europe.

Context aside, specific questions have always remained about why the LSE remained aloof for so long, and why it has chosen to pursue only select alliances over the past eight years. Why, in the face of so much global change and decisive action by its American and European counterparts did LSE continue to operate alone? Why did it ignore advances that would have rendered it one of the largest exchanges in the world? Was the LSE remaining solitary out of stubbornness and internal resistance to change, because of some grand strategic plan or as a result of a series of perhaps unhappy coincidences?

While there are some aspects of the answers to each of these questions that may remain behind closed doors, this chapter seeks to address them. The broader context and history of the LSE, when read in light of the events and commentary surrounding each attempted

* The author would like to acknowledge, in particular, the assistance of James Sainty with this chapter.

¹ LSE, or 'the Exchange' hereinafter.

merger, whether a success or a failure, provide the basis to argue that there are two primary reasons that explain the LSE's trajectory over the past 17 years.

First and foremost, the LSE's overt 'policy of independence', demonstrated by an 'attitude', with roots in the 'clubbiness' of the Exchange. It is this attitude, or self-belief, which accounts for the Exchange's initial resistance to change. After compromises with the government were reached in the early 1980s, resistance to change softened to hesitation. The Exchange was tentative, almost nervous, and began to explore ways of participating in the new international markets, without relinquishing the safety of home.

Finally, beginning in 2000, as offers to merge began to pour in, the LSE began to view its sense of independence as a help, not a hindrance. At the centre of one of the capitals of global finance, with strong domestic ties and access to the world's major financial intermediaries, the LSE came into its own. Biding its time, somewhat courageously in the face of falling profits, through several large bids, many of which could have seen it lose its independence, the Exchange finally made its first move in 2007. Since then, nothing has impeded its progress, and the 2014 acquisition of Frank Russell Company, the American company with a stock index business including the Russell 2000, shows that the LSE is as confident and as diversified but still as independent as ever.

Secondly, a clutch of heterogeneous reasons goes some way to explaining the difficult and fraught merger negotiations involving the LSE. In the category of factors leading to failure are: unsuccessful merger strategy (including corporate governance failures on the part of merger partners), under-valuations of the LSE and lack of, or insufficient, business synergies. These three factors, in various guises, operated in each of the failed mergers or breakdowns in negotiation between LSE and OMX, Deutsche Borse (twice), NASDAQ (several times), Macquarie Bank and TMX. Moreover, many discussions between the LSE and other exchanges that went unreported in the media or put to one side in the commentary are likely to have failed for similar reasons.

In the category of factors leading to merger success stories, are trading technology and the diversification of exchange business lines into pre- and post trade services. The LSE has reacted in a leisurely, non-coerced, manner, looking for considered and symbiotic relationships.

II CONTEXT: LEAD UP TO THE 21ST CENTURY

A The Big Bang

From World War II until 1979, the presence of exchange controls, introduced to stabilize the sterling, had ‘cocooned’ the members of the LSE from international competition.² The removal of these controls in 1979 suddenly incited UK residents to purchase foreign securities, foreign investors to buy British securities and London to become a convenient centre of finance for institutional investors from around the globe.³

Foreign intermediaries flooded into the City of London, sparking outrage swept. There were claims that international capitalism had trumped democracy.⁴ These foreign intermediaries established themselves and began to run a foreign investment market. The LSE’s control over the domestic market (which had been divided from this foreign market thus far) began to slip.⁵

Only the largest firms of brokers envisioned the international potential of European securities, and the role London could play in this. Many of the old guard members of the LSE had never been required to concern themselves with business in foreign securities or foreign clients. They feared alteration of the regulations and rules that underpinned their control of the domestic market.⁶

This competitive shift saw the LSE forced to review its rules and regulations throughout the early 1980s, particularly in relation to single capacity and fixed commissions. As this process began, a case in the Restrictive Practices Court brought by the government (the RPC case) served to complicate matters. The case alleged that the LSE was exploiting a ‘quasi-monopoly’, and threatened to undermine the LSE’s already precarious hold on the domestic market. The Exchange’s entire rulebook risked being thrown out, jeopardising the LSE’s

² Ranald C Michie, *The London Stock Exchange: A History* (Oxford University Press, 1st ed, 2001) 500.

³ Ibid 521.

⁴ David Kynaston, *The City of London: Volume IV – A Club No More, 1945-2000* (Pimlico, 1st ed, 2002) 585.

⁵ Michie, above n 2, 544.

⁶ Ibid 524.

institutional role and the stability of the market as a whole.⁷ As the Exchange at this point was the primary, if not exclusive, regulatory body, its role was crucial.

Attempts by the Council of the LSE to persuade the government to drop the case were futile. The Thatcher government's reluctance to compromise was based upon a concern that any concessions would be viewed by the public as a conservative government 'pandering' to their friends in the City of London.⁸ However, several years later, as the date for the case was set and the Exchange was forced into a corner, a deal was struck. Four weeks of negotiation between the Exchange and the government prompted an agreement to: 'dismantle, by stages and with no unreasonable delay, all the rules which at present prescribe minimum scales of Commission, and to complete the dismantling by 31 December 1986'.⁹

The Exchange also agreed to expand their policy on membership applications and to become more accountable to non-members. The Council was to include non-members appointed by the Bank of England. Not long after, the RPC case adjourned, and eventually legislation was passed exempting the Exchange from the RPC's jurisdiction.¹⁰

The Big Bang resulted from the confluence of two forces: (i) as Ranald Michie suggests, the 'power of impersonal market forces, whereby technological change and globalization destroyed the natural protection of a national stock exchange'¹¹ and (ii) the political agenda of the conservative Thatcher government, which pushed the Exchange into compromise. To achieve their goal of unleashing the forces of the free market and globalization, the Thatcher government was prepared to let slip the LSE's monopoly, and the Exchange's favour, in order to win public approval.

The compromises agreed upon in 1983 were implemented reasonably quickly in the three or so years leading up to the Big Bang, on October 27, 1986.¹² Reform of regulations relating to investor protection, including the Securities and Investment Board began in 1985. By mid-1985, the LSE had accepted that member firms could be 100% owned by single non-members (from March 1, 1986), which meant they could be full subsidiaries of British or

⁷ Ibid 545.

⁸ Ibid 548.

⁹ Ibid 550.

¹⁰ Ibid 553-4.

¹¹ Ibid 543.

¹² Kynaston, above n 4, 688-692.

foreign banks. On the Friday of the Big Bang, the LSE finally readied itself to enter the international market. After ‘20 semi-wasted years...it was time, at last, to get real’.¹³

B Mergers with ISRO and LIFFE

The first significant move made by the Exchange after the Big-Bang was to merge with the International Securities Regulatory Organization (ISRO) in September 1986. This merger is explicable by looking to the conditions the Bang created in the City. After the Big Bang, many of the LSE’s member firms had become foreign owned. Many international companies, attracted by SEAQ International, had also flocked to the Exchange in order to benefit from the orderly market provided by the new rules.¹⁴ The merger with ISRO was done to address this new international focus, with two purposes in mind. The first was to establish a self-regulatory organisation (SRO) under the new legislation.¹⁵ The second was driven by the fact that many of the ISRO firms trading in the Eurobond market had become members of the exchange under the new rules. As such, the merger drove international players towards the Exchange, rather than leaving it open for them to go and form a separate organisation and market.¹⁶

There was, however, possibly a third purpose to the ISRO merger. Many figures in the financial world, particularly those based in New York, recognised that the merger not only sought to create a 24 hour electronic marketplace for stocks, but would allow the Exchange to self-regulate and to provide trading options in around 100 American blue chip equities.¹⁷ That is to say, the merger with ISRO proceeded on the basis that LSE saw themselves, in this new world order, as a genuine competitor of New York in claiming to be the global centre of finance. In April 1988, the merger with ISRO took effect, and the LSE was permitted to both regulate the market and the conduct of participants. By merging with ISRO, the LSE brought the large number of international players streaming into London under the Exchange’s purview, as well enhancing the Exchange’s status around the world.

¹³ Ibid 697-8.

¹⁴ Michie, above n 2, 580.

¹⁵ *Financial Services Act 1986* (UK) c 60.

¹⁶ Michie, above n 2, 581-2.

¹⁷ ‘London Stock Exchange Seeks Global Role’, *Associated Press News Archive* (online), 16 September 1986 <<http://www.apnewsarchive.com/1986/London-Stock-Exchange-Seeks-Global-Role/id-2c0b99ae65781887731eb878dea615dc>>.

This self-important vision of the LSE played out again in its attempt to purchase the London International Financial Futures and Options Exchange (LIFFE) in 1987.¹⁸ LIFFE was established in 1982 when exchange controls were lifted, and it began trading futures and options. At the time of the attempted takeover, LIFFE was developing a contract based on German government bonds, which eventually provided a disincentive to merge with LSE.¹⁹ Michie suggests LIFFE harboured concerns about its autonomy if subsumed as just one component of a hypothetical London Futures and Options Exchange. This, he suggests might have spurred LIFFE to fear that a tie up with the LSE would stifle LIFFE's 'entrepreneurial' operation.²⁰

Eventually the LSE seemed to reconcile LIFFE's rejection of the Exchange's advances with its future strategy, although it would not stop future attempts to merge with the lucrative and forward thinking exchange.²¹ LIFFE's interest in the LSE's Options Market (LTOM) caused the LSE to identify that by putting more energy into developing their Options market further, they could seek to become a dominant force in that field in their own right. This view, interestingly, changed a few months later, when the Council decided that the LSE should focus on becoming the most important market for international equities, and that the futures markets could be left alone. This decision was likely prompted by the crash of October 1987.²²

As such, the remainder of the 1980s saw the LSE being only partly successfully in attempting to regain its dominant position in the world order, absent the advantages of a quasi-monopoly. While the absolute dominance of days gone past were likely gone forever, the Exchange had unequivocally established that they were still the dominant force in the domestic market and were holding more than their own in the international equity markets.

The scope for expansion in the domestic market was clearly limited due to the operation of LIFFE, but the merger with ISRO paved the way for international expansion. This was facilitated in part by the replacement of the trading floor with an electronic network and by the extension of membership to a variety of major global financial players. As the European forerunner of electronic trading, through SEAQ International, the LSE was able to assert

¹⁸ David Kynaston, *LIFFE: A Market and its Makers* (Granta Editions, 2002) 152.

¹⁹ Michie, above n 2, 582.

²⁰ Ibid.

²¹ Simon English, 'Garban Chief Rejects LSE Plans for Liffe Merger', *The Telegraph* (London), 31 May 2001.

²² Michie, above n 2, 583.

initial post-Big Bang dominance, through their preparedness to quickly abandon the trading floor.²³

The 1990s saw the future of all physical stock exchanges put into serious question.²⁴ The LSE was in the doldrums. Many saw the Exchange as directionless at best, or incompetent at worst,²⁵ as the waves of globalisation eroded the bricks and mortar exchanges.²⁶ However, in 1995 the LSE launched the Alternative Investment Market (AIM), an international market for growing companies. This was in a way a response to the criticism directed at the Exchange's future redundancy over the early 1990s, and a good one at that; by 1996 the AIM had 205 securities listed on it, at a value of 4.3 billion pounds.²⁷ The second event – and response to the criticisms – of the 1990s was the LSE launching their Stock Exchange Electronic Trading Service, in 1997. This was designed to enhance the speed and efficiency with which market trading could occur.²⁸

Finally, July 1999 saw the LSE membership vote to demutualize and become a publicly listed company, operating a fully commercial basis. The exchange saw this as necessary as a result of the increasing competition being created by the advent of electronic trading.²⁹ It was widely viewed as the final practical step away from the 'club' structure formed nearly exactly 200 years earlier, in 1801.³⁰

Demutualisation occurred in March 2000, and one year later, the Exchange listed on itself, attracting a market capitalisation of approximately \$2.1 US billion. Amid concerns over conflicts of interest, the Exchange relinquishing its role as a regulator of the primary market to the Financial Services Authority, allowing the Exchange to place its customers and shareholders at the centre of its activities. Additionally, the Exchange gained the flexibility it needed to operate in a rapidly changing environment.³¹

²³ Norman S Poser, 'The Stock Exchanges of the United States and Europe: Automation, Globalization and Consolidation' (2001) 22 *University of Pennsylvania Journal of International Economic Law* 497, 502.

²⁴ Richard O'Brien, *Global Financial Integration: The End of Geography* (Chatham House, 1992) 8.

²⁵ See Erik Portanger and Vanessa Fuhrmans, 'How it Became a Foggy Day on the London Exchange', *Wall Street Journal* (New York), November 2 2001, 1; Vincent Boland, 'Securing a Future', *Financial Times* (London), March 5 2001, 22.

²⁶ J J Fishman, *The Transformation of Threadneedle Street: The Deregulation and Regulation of Britain's Financial Services* (Durham, NC, 1993) 269.

²⁷ Michie, above n 2, 619.

²⁸ London Stock Exchange, *Our History* (7 July 2015) <<https://web.archive.org/web/20150905191913/http://www.londonstockexchange.com/about-the-exchange/company-overview/our-history/our-history.htm>>

²⁹ Laura Padilla Angulo, 'The London Stock Exchange: Strategic Corporate Governance Restructuring After Demutualization' (2014) 30(1) *The Journal of Applied Business Research* 211, 216.

³⁰ Ibid 215.

³¹ Ibid 215-6.

III POLICY OF INDEPENDENCE

Against the backdrop of the Big Bang, the internationalisation of the City, the launch of AIM and demutualisation, between 2000 and 2006 the LSE pursued a policy of independence or self-imposed isolation. The Exchange resisted takeover attempts and merger proposals from the Continent (Euronext, Deutsche Borse and OM Group), across the Atlantic (NASDAQ) and even from Australia (Macquarie Bank). What accounts for such frenzied activity?

First, London was an incredibly attractive merger partner. In 2000 the LSE was the largest stock exchange in Europe, with a market capitalisation of \$2.9 trillion US dollars, an impressive listing of both domestic and foreign companies and a trading book of upwards of 12000 securities.³² This preeminence may have given the LSE a false sense of security, that nothing had changed despite the shake-up of the Big Bang; it could continue to go it alone. Or perhaps the LSE may simply have been biding its time, reluctant to compromise its prized autonomy.

Secondly, many of the proposals the LSE received were deficient in various ways, thwarted in particular by shareholder and regulatory concerns. Each negotiation was marked or interrupted by some tangible disincentive for the LSE to proceed.³³ Suitors themselves had their own ambitions for global branding and dominance, putting them at odds with those of the LSE.³⁴

OMX Group and the LSE did successfully cooperate to create EDX London, an international equity derivatives business. However, LSE relinquished no independence in the creation of EDX and benefited from the technological savvy of the Nordic exchanges.³⁵ London's suitors went elsewhere, at least temporarily. London did not form part of the 'mega-exchanges' NYSE Euronext or NASDAQ OMX Group.

A Deutsche Borse – the 'First Failure'

In 1998, the LSE had entered into talks with Deutsche Borse (DB), the Frankfurt based stock exchange which resulted in an alliance, with a view to creating a common electronic trading

³² Poser, above n 23, 502.

³³ 'Hard to Get', *The Economist* (London), 16 July 2005, 71.

³⁴ David Fairlamb, 'Swedish Surprise: OM's bid catches the London Stock Exchange off guard', *Business Week*, 11 September 2000, 58.

³⁵ 'London Stock Exchange and OM to Create new Equity Derivatives Business' *OM* (Sweden), 9 December 2002.

platform.³⁶ This alliance continued until May 3, 2000, when the LSE and DB announced a long awaited merger. At the time of this announcement, it was ground-breaking, ‘the most far-reaching undertaken by any stock exchanges’.³⁷ The plan for the two companies was to merge their cash markets in equities and derivatives into a company called ‘iX’, to stand for International Exchanges.³⁸ If it had gone ahead, it would have created the world’s third biggest stock market by turnover, and easily the largest in Europe.³⁹ Clearly the merger would have established an enormous exchange with numerous ostensible advantages. Importantly, it would have beaten every other exchange to the punch, and likely become the first pan-European market.⁴⁰

Despite this, the DB-LSE tie up was not to be. A litany of reasons caused the merger to fail, some of which can be linked to the LSE’s insistence on independence. However, many of the obstacles to the creation of iX were simply unfortunate coincidences, or tactical errors on the part of DB.

London was wary of DB’s aggressive CEO, Werner Seifert, who was to head up iX.⁴¹ On the other hand, certain aspects of the plan were too London-centric. Blue chip stocks were to be confined to trading in London,⁴² while Frankfurt would trade smaller growth companies, which had been the preserve of AIM.⁴³ The LSE’s insisted on being the headquarters of the merged entity, arguing that only London could compete with New York City.⁴⁴ Despite the relative arbitrariness of this it became a sticking point that exacerbated tensions, particularly in light of DB’s demands for management control.⁴⁵

Secondly, the business plan for iX failed to articulate several key aspects of the merger. It omitted to identify processes or mechanisms to deal with the differences in regulatory systems, practices and currency.⁴⁶ It also neglected to explore how a proposed secondary venture with NASDAQ would actually play out.

³⁶ Francis A Lees, *Financial Exchanges: A Comparative Approach* (Routledge, 1st ed, 2012) 133.

³⁷ Vincent Boland and Aline van Duyn, ‘Deal with London Gives Frankfurt Added Weight: Deutsche Borse’, *Financial Times* (London), 22 May 2000, 12.

³⁸ Poser, above n 23, 503.

³⁹ Boland and van Duyn, ‘Deal with London Gives Frankfurt Added Weight: Deutsche Borse’, above n 37.

⁴⁰ Poser, above n 23, 503.

⁴¹ Ibid; see also ‘London Stock Exchange and OM to Create new Equity Derivatives Business’, above n 35.

⁴² Poser, above n 23, 503.

⁴³ Lees, above n 36, 133-4.

⁴⁴ Ibid 134.

⁴⁵ Boland, Vincent and Aline van Duyn, ‘iX Doubt Creeps Out: Vast Detail on the Planned Merger of the London Stock Exchange and Deutsche Borse Has Not Been Enough to Deflect Dissent’, *Financial Times* (London), 22 May 2000, 30.

⁴⁶ Boland and van Duyn, ‘Deal with London Gives Frankfurt Added Weight: Deutsche Borse’, above n 37, 13.

Thirdly, shareholder opposition in both London and Frankfurt proved problematic. The owners of DB, an aggressive and tightly knit syndicate of leading German banks, wanted as much control as possible for DB.⁴⁷ There were issues of questionable corporate governance at the German exchange. Several LSE member-shareholders were loathed to lose trading in growth stocks;⁴⁸ others were critical of a poorly thought out merger.⁴⁹

Costs were an issue in this ‘first failure’. The merger would have replaced two successful, extant exchanges with two new ones, but increasing the costs to both.⁵⁰ Settlement, the single biggest cost to cross-border trading at the time, was not addressed in the merger plan.⁵¹ The leak of an internal memo telling LSE staff to ‘blame the Germans’ in an event of breakdown further served to obfuscate discussions and compromise the viability of the merger.⁵² Then the OM Group entered the fray with a competing offer in August 2000.⁵³

The LSE had entered the takeover game.⁵⁴ However, the talks between the London and Frankfurt had also spurred the creation, in September 2000, of another, different, pan-European exchange, Euronext, following a merger of the Amsterdam Exchanges, Brussels Exchange and Paris Bourse.⁵⁵ Symbolically at least, Euronext was a blow to the LSE. iX had been intended to be a pan-European stock market. Euronext beat LSE to the punch while claiming the status of the ‘first integrated European stock and derivatives market’.⁵⁶ Then, in 2001, Euronext’s acquisition of LIFFE added further insult to injury.⁵⁷

B OM Group

The surprise bid of August 2000 by OM Group was a final piece of excitement for the LSE in what had already been an eventful year.⁵⁸ A friendly bid was made first, which the LSE rejected. The next week, OM Group followed up with a hostile bid. The offer, not surprisingly, was at a significant premium of GBP3.50 per share, in a cash and share

⁴⁷ Boland, Vincent and Aline van Duyn, ‘iX Doubt Creeps Out’, above n 45.

⁴⁸ Poser, above n 23, 503.

⁴⁹ James Moore, ‘LSE Merger Flawed, Says Old Mutual’, *The Times* (London), 6 September 2000, 25.

⁵⁰ Lees, above n 36, 134.

⁵¹ Charles Pretzlik and Aline van Duyn, ‘London Takes Stock: A Swedish Takeover Approach for the London Stock Exchange Highlights Unresolved Issues in the Way of a Merger with Germany’s Deutsche Boerse’, *Financial Times* (London), 29 August 2000, 16.

⁵² Amanda Hall, ‘Steely Don’ [2000] (June) *Director* 45, 45.

⁵³ Erik Portanger, ‘Exchange in London Now in Play’, *Wall Street Journal* (New York), 30 August 30 2000, A18.

⁵⁴ Lees, above n 36, 134.

⁵⁵ Ekaterina Dorodnykh, *Stock Market Integration: An International Perspective* (Palgrave Macmillan, 2013) 30.

⁵⁶ Poser, above n 23, 504.

⁵⁷ Dorodnykh, above n 55, 30.

⁵⁸ Hall, above n 52.

exchange: GBP20 in new OM shares plus GBP7.19 in cash.⁵⁹ There were some suggestions that the bid was a defensive move to impede the iX merger, rather than a genuine attempt at fostering a successful joint enterprise with London.⁶⁰

Despite the strong position and technology focus of the OM Group, the LSE initially described the bid as unattractive – at least relative to the iX merger. With the advent of the hostile takeover, OM Group began a roadshow throughout October 2000, visiting LSE shareholders, trying to garner their support.⁶¹ The OM Group conceded defeat in early November, when only 6.7% of shareholders indicated support.

Two failed mergers in such a short period of time impacted the credibility of the executive ranks at LSE, leading to the replacement of CEO Gavin Casey. The shareholders' general opposition – and level of animosity towards Casey immediately prior to his replacement – reflected negatively on the LSE's foreign merger prospects.⁶²

Why did LSE shareholders reject the OM Group bid? There was suspicion at the time as to the motives of the OM Group, that their interest was driven primarily by the publicity and recognition associated with the bid.⁶³ As with the proposed DB merger, London feared losing its position as the centre of European international finance and OM Group would not bring with it a burgeoning derivatives market. LSE shareholders may also have been holding out for a sweeter deal should a “white knight” appear to spur better terms from DB or Euronext.⁶⁴

C EDX

Nevertheless, 2003 saw the rekindling of the OM LSE relationship, and with it, the formation of EDX London, an international equity derivatives business, capitalising on London's strong international equity presence and the technological prowess of the Nordic group. Announced late in 2002,⁶⁵ the move signaled a slight softening in the LSE's ‘policy of independence’ in going back to OM, after fending off their hostile bid. Clara Furse, who the media regarded as

⁵⁹ ‘London Stock Exchange and OM to Create new Equity Derivatives Business’, above n 35; Fairlamb, above n 34.

⁶⁰ ‘LSE Quick to Dismiss OM Groups's 808M Bid’, *The Scotsman* (Edinburgh), 29 August 2000 <<http://www.scotsman.com/business/finance/lse-quick-to-dismiss-om-group-s-163-808m-bid-1-838933>>.

⁶¹ Sheila Jones, ‘OM Roadshow Fails to Convince Regions: Stock Exchange Concerns Over Share Offer Remain’, *Financial Times* (London), 26 September 2000, 3.

⁶² Simon English, ‘Casey Falls on his Sword’, *The Telegraph* (London) 16 September 2000.

⁶³ ‘Modernizer Plots London Takeover’, *Euromoney*, October 2000, 42.

⁶⁴ ‘LSE Quick to Dismiss OM Groups's 808M Bid’, above n 60.

⁶⁵ Andrew Cave, ‘Old Rivals Forge New Derivatives Alliance’, *The Telegraph (UK)*, 10 December 2002; John Carroll, ‘London Stock Exchange Nabs a Competitive Edge: Derivatives Game Plan Targets European Players’, *Bank Technology News*, January 2003, 14.

the capable replacement for the somewhat derided Gavin Casey,⁶⁶ led the charge in looking to compete with LIFFE.

The formation of EDX London was designed to give the LSE a strong position in the lucrative derivatives market controlled at the time by LIFFE (owned by Euronext) and Eurex (owned by DB). EDX had the technological advantage of OMX, and looked to not only control Scandinavian equity derivatives but to leverage the technology to offer a wider set of products to a wider set of customers. Onlookers at the time suggested that rather than being a significant strategic change, the move was a growth initiative, not designed to – and not likely to – immediately threaten LIFFE.⁶⁷ This was confirmed by Clara Furse, who suggested at the time that EDX was created to provide services to the firms conducting the OTC market.⁶⁸

Not an obvious strategy even at the time of its creation, EDX quickly unravelled. In 2008 NASDAQ acquired OMX; most of the EDX derivatives contracts moved to NASDAQ OMX, leaving only the Norwegian derivatives products with EDX London.⁶⁹ These contracts were quietly rolled into the Turquoise trading service established by the LSE in 2009.

D DB's Second Bid and Euronext

As interest in a pan-European exchange persisted and London's international equities business went from strength to strength, the LSE became an ever more attractive prospect. In 2004, \$5.3 trillion in stocks traded in London and 293 initial public offerings took place over the exchange.⁷⁰ For these reasons, DB and the LSE put aside their differences and resumed discussions. Concurrently, Euronext entered the fray. London's \$5.3 trillion in stocks traded in 2004 exceeded the combined total of stocks traded on DB and Euronext for that year.⁷¹ For DB, the prospects of success had improved, in part due to the arrival of a new LSE head, Clara Furse and also because the LSE was no longer dominated by trading members. With

⁶⁶ Vincent Boland, 'A Single Minded Manager', *Financial Times* (London), 27 January 2001; Silvia Ascarelli, 'London Bourse is Set to Trade Tradition for Neutrality, Naming Outsider as CEO', *Wall Street Journal* (New York), January 24 2001.

⁶⁷ Carroll, above n 65.

⁶⁸ Jill Treanor, 'Stock Exchange Teams Up with OM', *The Guardian* (online), 10 December 2002 <<http://www.theguardian.com/business/2002/dec/10/3>>.

⁶⁹ 'Taking on the Big Boys – Nicolas Bertrand Interview', *Futures and Options World*, 23 July 2010 <<http://www.fow.com/2637010/Taking-on-the-big-boys-Nicolas-Bertrand-interview.html>>.

⁷⁰ Beth Carney, 'The London Exchange's Last Days?', *BusinessWeek Online*, 2 February 2005 <<http://www.bloomberg.com/bw/stories/2005-01-30/the-london-exchanges-last-days>>.

⁷¹ Ibid.

demutualisation, most of LSE's new shareholders were only interested in obtaining the best price for their investment.⁷²

The DB bid, for 2 billion euro (GBP 1.3 billion), launched on December 13, 2004, valuing the LSE at a 23% premium over its closing price two days earlier. The LSE rejected the bid as too low, but DB kept the bid open over the following three months.⁷³ Meetings between Clara Furse, Weiner Seinfert (head of DB) and head of Euronext ensued. Discussions continued until February 9, 2005, at which point a 5% activist shareholder (The Children's Investment Fund, or TCI) took DB out of the game.⁷⁴ TCI cited a failure of corporate governance on the part of CEO Werner Seifert,⁷⁵ who was promptly replaced by the hedge funds that had brought the deal down.⁷⁶ The Euronext talks eventually came to nothing, despite promising signs.

By this stage, the LSE policy of independence had already begun to weaken (partly due to Furse's influence), being replaced by a tacit acknowledgement that something had to happen soon.⁷⁷ It is unclear whether the LSE's extended talks with the German Börse were genuine or merely posturing so as to generate interest from Euronext and perhaps the exchanges across the Atlantic. Regardless, LSE was clearly in the driver's seat, due to a market share that dwarfed its two competitors

Despite the failure of the merger, the talks piqued the interest of the British authorities as to the regulatory consequences of a pan-European merger. In April 2005, an investigation was conducted by the British Competition Commission about the consequences of any hypothetical mergers between the LSE and Euronext or DB. The competition issue raised by a merger with DB was clearing and settlement: LCH Clearnet would become the sole provider of settlement and clearance services, potentially triggering provisions about

⁷² Richard Wachmann, 'German Invasion- Or Just a Case of Market Economics?', *The Guardian* (online), Sunday 19 December 2004 <<http://www.theguardian.com/business/2004/dec/19/theobserver.observerbusiness17>>.

⁷³ Carney, above n 70.

⁷⁴ Ibid.

⁷⁵ See Sudi Sudarsanam and Tim Broadhurst, 'Corporate Governance Convergence in Germany through Shareholder Activism: Impact of the Deutsche Boerse Bid for London Stock Exchange' (2012) 16 *Journal of Management and Governance* 235; and Stilpon Nestor, 'How Bad Governance Cost Deutsche Börse Its Deal', *International Financial Law Review* (online), 1 October 2005 <<http://www.iflr.com/Article/1984711/How-bad-governance-cost-Deutsche-Brse-its-deal.html>>.

⁷⁶ David Lanchner, 'Lull Before the Reform?' (2005) 30(5) *Institutional Investor International Edition*, 14, 17.

⁷⁷ 'Hard to Get', above n 33.

substantial lessening of competition.⁷⁸ The report concluded that the DB merger would not lead to any substantial lessening of competition.⁷⁹

The merger also piqued the interest of the Association of Private Client Investment Managers and Stockbrokers (essentially an organisation comprised of the big banks), as well as regulators and companies listed on AIM. The mergers, some argued, had it gone ahead, could usher ‘in an era of lower costs for European exchange users and greater profits for bourse investors.’⁸⁰ European Securities Forum representatives suggested that the bid drew people’s minds to the questions of competition across Europe, and could accelerate the harmonisation of regulation and consolidation among the exchanges.⁸¹ Onlookers were optimistic that a ‘lucrative equilibrium struck between profit-driven exchange shareholders and efficiency and cost-driven users’.⁸² The regulatory clearances that the failed attempts engendered, were arguably important signposts of the pan-European regulation and integration that was to follow.

E Macquarie

Yet another offer for the LSE came late in 2005 from the Australian Macquarie Bank (Macquarie), after some degree of build up and speculation.⁸³ Macquarie offered GBP 1.5 billion or 580 pence per share, which it characterized as attractive. Macquarie quickly became hostile after LSE’s board balked.

The Macquarie price appeared, simply, too low - the LSE described it as ‘derisory’ – and that the businesses lacked synergies. The LSE issued a statement that the proposal lacked strategic or commercial credibility.⁸⁴ The fact was, in light of attempts by Euronext and DB failing, Macquarie’s offer clearly fell outside the scope of the sort of relationship the LSE was striving to develop. Geographic factors aside, Macquarie brought none of the diversity the LSE sought in derivatives or clearing services. The LSE would have had to relinquish its cherished “independence”, a notion which may have evolved under Furse, but which

⁷⁸ ‘Stock Exchange Mergers: Three Dimensional Chess’, *The Economist* (London), 4 August 2005.

⁷⁹ *Competition and Markets Authority Case: London Stock Exchange plc/Deutsche Borse AG and Euronext N.V. Merger Inquiries* (1 November 2015) <<https://www.gov.uk/cma-cases/london-stock-exchange-plc-deutsche-b-rse-ag-and-uronext-n-v-merger-inquiries-cc>>.

⁸⁰ Lanchner, above n 76, 14.

⁸¹ *Ibid* 16.

⁸² *Ibid* 19.

⁸³ ‘LSE Receives “No Formal Approach” from Macquarie Bank’, *Australian Broadcasting Corporation*, 15 August 2005 <<http://www.abc.net.au/news/2005-08-15/lse-receives-no-formal-approach-from-macquarie-bank/2081538>>.

⁸⁴ ‘LSE Rejects “Derisory” Bid by Macquarie Bank’, *Australian Broadcasting Corporation*, 15 August 2005 <<http://www.abc.net.au/news/2005-12-10/lse-rejects-derisory-bid-by-macquarie-bank/758472>>.

remained very much part of the LSE ethos and identity. Macquarie argued that DB and Euronext had both lost interest and that a merger with a US exchange was unlikely to be allowed by the US regulator, the SEC.⁸⁵

Fundamentally, the bid failed because of divergent views over the value of the LSE.⁸⁶ Macquarie saw the LSE as a low-growth business with a cyclical operation. LSE shareholders saw high growth potential due to increased volumes generated by high frequency trading. The DB and Euronext discussions had also stoked the price expectations of the LSE shareholders.

F NASDAQ

Speculation in 2002 and ongoing talks from 2004 preceded a NASDAQ acquisition bid in 2006. NASDAQ was motivated by same factors which had attracted European suitors, with the difference that the NASDAQ overtures came from across the Atlantic.⁸⁷ Only months later, NYSE and Euronext successfully merged to create the first large scale trans-Atlantic exchange.

London's AIM market was also competing with NASDAQ for listing early-growth companies⁸⁸ and the LSE's large investment in high speed trading systems presaged even greater future competition.⁸⁹ Status and size also mattered. NASDAQ wanted to win the race to be the first transatlantic exchange, with operations in both major centres of global finance. The synergies were attractive; the merger would 'unite the premier market for technology companies in the USA with one of the oldest venues for share trading with Europe'.⁹⁰ It would have created the world's second largest exchange, with more than 6000 companies listed and aggregate market capitalization of \$7 trillion.⁹¹

Despite all the speculation in the 4 years leading up to it, NASDAQ's initial 4 billion US dollar offer to the LSE, in March 2006, was rejected. As with the Macquarie bid, it may have

⁸⁵ Norma Cohen, 'Macquarie Abandons Bid for London Stock Exchange', *Financial Times* (London), 20 February 2006 <<http://www.ft.com/intl/cms/s/0/93ed699a-a24c-11da-9096-0000779e2340.html#axzz3fNpy7UET>>.

⁸⁶ Ibid.

⁸⁷ Michael Gorham and Nidhi Singh, *Electronic Exchanges: The Global Transformation from Pits to Bits* (Elsevier Financial Markets Press, 1st ed, 2009) 172-3.

⁸⁸ A Postelnicu and D Blackwell, 'Take Aim and Outshine the Competition', *Financial Times*, 3 September 2005, 9.

⁸⁹ Lees, above n 36, 148.

⁹⁰ Aaron Lucchetti and D Reilly, 'London Exchange Rebuffs a Bid from NASDAQ', *Wall Street Journal* (New York), 11 March 2006, B1.

⁹¹ Lees, above n 36, 146.

simply been an undervaluation of the LSE, failing to reflect a number of supposedly “hidden values” such as technology synergies⁹² and the value of control ownership.⁹³

After the rejected bid of 2006, NASDAQ acquired a 30% stake in LSE and by January 2007 the NASDAQ offer stood at USD5.7 billion. This offer too was rejected, in part due to constraints imposed by the UK Takeovers Panel rules.⁹⁴

The LSE viewed their business model as incompatible with that of NASDAQ. While impressive, NASDAQ’s listings were primarily the smaller technology companies; the LSE saw its reputation and prestige deriving from its status as a global financial centre in the same league as the NYSE.⁹⁵

Secondly, the LSE already had a viable smaller growth company market in AIM which, over the period 2003 through 2007 had attracted many non-UK companies.⁹⁶ Although half the size of NASDAQ, many companies preferred AIM as it offered lower listing costs (4 to 5% of capital raised as compared to 6 to 8% for NASDAQ). For small, capital hungry companies, this was a big difference. AIM had been a primary attraction for NASDAQ, but proved a sticking point for the LSE.⁹⁷

In addition to the perceived lack of synergies, the merger discussions were confounded by a rising LSE share price. From March 2006 to February 2007, the share price of the LSE was increasing rapidly in contrast to NASDAQ’s which was plateauing. LSE further exacerbated matters by engaging in a variety of strategic manoeuvres, such as share repurchases and cost controls, which provided incentives to shareholders not to part with their shares.⁹⁸ More importantly, the LSE was extremely reluctant to be regulated by the SEC.⁹⁹

The NASDAQ discussions also coincided with the LSE introducing a high-speed trading platform. This platform was called TradElect and offered algorithmic trading to users. It was

⁹² J Authers, ‘Platforms Hold Key to Merger Savings’, *Financial Times*, 16 March 2006, 21.

⁹³ Lees, above n 36, 147.

⁹⁴ A McDonald and H Teitelbaum, ‘NASDAQ Declines to Raise its Bid for LSE’, *Wall Street Journal* (New York), 27 January 2007, B3.

⁹⁵ Dorodnykh, above n 55, 37.

⁹⁶ Such as EBT Mobile, a company from China, which Lees suggests enrolled on the AIM despite ‘a more neutral home’ for it would have been NASDAQ; Lees, above n 36, 146.

⁹⁷ *Ibid.*

⁹⁸ ‘Nasdaq Fails in Takeover Bid for London Stock Exchange – Business – International Herald Tribune’, *The New York Times* (online), 11 February 2007 <<http://www.nytimes.com/2007/02/11/business/worldbusiness/11iht-nasdaq.4549290.html>>.

⁹⁹ Gorham and Singh, above n 87, 173; Grant Ringshaw, ‘LSE and NASDAQ Seek Merger Concessions’, *The Sunday Telegraph*, 2 June 2002.

able to display prices within 2 milliseconds of receipt, and served to greatly improve and modernise the LSE's internal trading and information services.¹⁰⁰

Finally, the LSE was at the time, holding discussions with Borsa Italiana. The Italians had signalled their interest around the same time as Macquarie and NASDAQ, and had received an initially negative response. However, in this fluid and dynamic environment things could change quickly.¹⁰¹

So why did the LSE choose to reject a powerful rival, to merge with the smaller, relatively insignificant Milan exchange? The rush of mergers between exchanges had been intense in the prior years. Competition was taking its toll on the LSE; profits were falling, despite a rising share price. The introduction of TradELECT had been expensive but necessary. London was struggling to gain ground on New York as the centre of world finance, particularly since the NYSE-Euronext merger had gone ahead. For all its strengths, the LSE lacked diversity in its revenue streams (it had no strong derivatives business), was not operating its own clearing house (compared to exchanges like Deutsche Börse) and found its profit margins being squeezed by ECNs and even smaller exchanges like Switzerland's.

In this context, the merger with NASDAQ must have seemed intuitively attractive to some shareholders of the LSE. It would have formed one of the world's largest exchanges and would have beaten the NYSE-Euronext joint enterprise to the punch. But to proceed with the merger would have been to ignore what the LSE really needed, which was diversified revenue. And the LSE found just that in the Borsa Italiana, located in Milan.

IV FROM THE HUNTED TO THE HUNTER

In 2007, the LSE shifted from being the hunted to being the hunter with the merger with Borsa Italiana, located in Milan. The LSE then went on to purchase an interest in Turquoise and merged it with Baikal to create a multilateral trading facility. Further investment in technology, with the purchase of MilleniumIT, occurred in 2009. In 2011, an aborted merger with the Canadian TMX group recalled the failures and near misses of the earlier decade, and revived rumours that, in an aboutface, the LSE might acquire NASDAQ.

A Borsa Italiana

¹⁰⁰ Lees, above n 36, 148.

¹⁰¹ Gorham and Singh, above n 87, 173-4.

Announced mid-way through 2007 amidst concerns that NASDAQ might attempt to block the merger, discussions with the Borsa Italiana (BI) had been ongoing since the approaches of Macquarie and NASDAQ in 2006. NASDAQ however had already abandoned their pursuit of the LSE and was looking to offload their substantial shareholding. In early 2008, the Qatar Investment Authority (QIA) purchased it in exchange for a stake in OMX.¹⁰² The QIA had ambitions to imitate the London exchange, in order to develop securities trading in the Gulf region.¹⁰³

Clara Furse, head of the LSE, justified the merger by citing increased earnings, accelerated stock listings and share trading in the Italian market and reputational advantages, all of which sound somewhat hollow.¹⁰⁴ Personalities also played a part. Massimo Capuano, a former McKinsey partner and an ambitious leader of the Borsa Italiana,¹⁰⁵ saw the strategic advantages in a pan-European exchange and wanted to block a trans-Atlantic merger between NYSE and Euronext. Despite his failure to realize either of his ultimate goals, he was a key driver in making the merger a success.

The most attractive element of the BI for the LSE was the Italian exchange's strong derivatives and bond trading platforms. BI was small compared to the LSE, only slightly smaller, in terms of the value of the domestic companies listed on it, than OMX or the Swiss exchange.¹⁰⁶ The merger with the LSE created Europe's largest stock exchange, with a widely diversified revenue stream. The Borsa Italiana brought to the table a 'sprawling group of businesses, including equities, derivatives trading, clearing, settlement and custody'.¹⁰⁷ It also had a large share of the MTS Bond trading platform, along with an option to seize full control from Euronext. Despite the low tariffs for trading, settlement and clearance, the Borsa had a profit margin of 38%.

The MTS bond trading platform, originally created by the Bank of Italy to trade Italian government bonds, was a particularly attractive acquisition. Borsa Italiana and Euronext owned the holding company in nearly equal measure, with the latter having the 51%

¹⁰² Gorham and Singh, above n 87, 174-5.

¹⁰³ Lees, above n 36, 117.

¹⁰⁴ Alistair Macdonald and A Mecenni, 'LSE Adds Dimension as Holders Back Deal', *Wall Street Journal* (New York), August 2009, 2007, C3.

¹⁰⁵ Gorham and Singh, above n 87, 173-4.

¹⁰⁶ Lees, above n 36, 150.

¹⁰⁷ *Ibid* 152.

controlling stake. With the merger, Borsa Italiana exercised its call option to acquire full control.¹⁰⁸

There were several other salient factors that attracted the LSE to the Borsa Italiana. One of them was the new stream of stock offerings, in the form of Italian medium sized family companies that would potentially become available to the LSE.¹⁰⁹ Whether any benefits materialized is unclear, although at the time ‘Italian bankers view[ed] the prospect of smaller Italian companies gaining the interest of large institutional money from London as a real possibility’.¹¹⁰

Francis Lees considers the Italian-LSE merger a success.¹¹¹ The merged group has the largest European equities pool by market capitalisation and by daily value of equities traded; the group is a primary listing venue, with the LSE consolidating its position as the first preference for large international companies while the merger with Milan increased access to European capital for those listing on the main market and on the AIM. Finally, Lees notes the increase in the efficiency of post-trade services that the group can now provide. Other commentators have pointed that the merger allowed the LSE to maintain its prized autonomy, while creating cross access opportunities and enlarged liquidity pools for both exchanges.¹¹²

The merger had not been a given. Hedge fund shareholders complained that a high value acquisition would dilute their interest in the LSE. Rumours circulated that NYSE Euronext, arguably a more desirable match than the LSE, had its eye on the BI.¹¹³

The LSE-Italiana merger could also be viewed as a ‘poison pill’, a purely defensive move by the LSE with a compliant partner in the BI. NASDAQ could have been poised to strike again, once the Takeover Panel rules allowed them to. The LSE merger with BI diluted NASDAQ’s stake. The perception remained that the LSE would only merge on its own terms, regardless of the business case.¹¹⁴

B 2009-09: *Turquoise and Baikal*

¹⁰⁸ Ibid.

¹⁰⁹ H Teitelbaum and C Emsden, ‘LSE to Gain Italy IPO Pipeline’, *Wall Street Journal*, 12 July 2007, C2 cited in Lees, above n 36; Dorodnykh, above n 55, 37.

¹¹⁰ Lees, above n 36, 152.

¹¹¹ Ibid 153.

¹¹² Dorodnykh above n 55, 37.

¹¹³ A Mocenni and E Taylor, ‘NYSE Makes Rival Bid for Borsa Italiana’, *Wall Street Journal*, 22 June 2007, C2.

¹¹⁴ Ibid 151, citing Norma Cohen, ‘Defensive Logic behind LSE’s Aggressive Italian Manoeuvre’, *Financial Times*, 23 June 2007, 9.

In 2008, the LSE revealed plans for a dark pool, to be called Baikal in homage to the deepest, darkest lake in the world, in the heart of Siberia. The market share of dark pools had been growing across North America in the preceding decade and Europe was following the trend. The LSE was shaking off its musty traditional image and keeping up with the times. DB launched its own dark pool, Xetra, later that year.¹¹⁵

Dark pools were a response to shifts in trading patterns. Algorithmic trading in equity markets by high frequency traders was forcing large investors such as superannuation and pension funds off the exchanges into the dark pools where large orders could receive special handling. In 2009, approximately one fifth of the equities traded in Europe each day was traded through a dark pool.¹¹⁶ Baikal was designed to provide the “special handling” for institutional investors trading in blue chip shares across continental Europe. Clearing was handled by the Borsa Italiana and the large buy-side traders accessed Baikal through the sell-side banks.¹¹⁷

In April 2009, Baikal selected Fidessa and BNP Paribas as technology partners to support Baikal. Cutting edge technology was essential in order to differentiate the business from the 12 other significant dark pools across Europe as at June 2009.¹¹⁸ The LSE also purchased MillenniumIT, a Sri-Lankan IT company, for 30 million dollars, with a view to developing new trading systems. These systems were to replace TradElect, the system introduced in 2007.¹¹⁹ Such a brief turnaround indicated the shortening of the technology cycle for stock exchanges, even in comparison to five years before.

In December 2009, LSE bought a 60% share in Turquoise, a multilateral trading facility (MTF) created by a syndicate of investment banks. Turquoise was set up and designed to allow trading to occur on and off traditional exchanges, at a 50% discount to ‘traditional’ stock exchanges. Once the purchase had gone ahead in February 2010, Turquoise was merged with Baikal, the LSE’s dark pool.¹²⁰ The LSE’s acquisition represented both an easing of tensions with the investment banks looking to offload Turquoise as well as an opportunity to offer trading across Europe.¹²¹

¹¹⁵ Ibid 154.

¹¹⁶ Ibid 155.

¹¹⁷ Jeremy Grant, ‘LSE Refreshes Baikal “Dark Pool”’, *Financial Times* (London), 16 June 2009.

¹¹⁸ Ibid.

¹¹⁹ Jeremy Grant, ‘LSE Buys MilleniumIT to Cut Costs’, *Financial Times* (London), 16 September 2009.

¹²⁰ Jeremy Grant, ‘LSE Buys Turquoise Share Trading Platform’, *Financial Times* (London), 21 December 2009.

¹²¹ Ibid.

By this time, Xavier Rolet had taken over from Furse as the CEO of the LSE Group.¹²² In one of his first press interviews, at the AGM that year, he indicated that the exchange was looking to provide services facilitating the trading of corporate bonds from Britain and across Europe. This was to supplement the current business the LSE Group had in Italian and other sovereign issued debt securities. Rolet was the instigator of the MilleniumIT purchase. He also helped to push through Baikal-Turquoise merger.

Revenues for the LSE Group declined in 2009, despite the merger of 2008. The global financial crisis no doubt contributed, but the relentless development of the preceding years and competitive pressures exerted by new technologically advanced stock trading platforms also played a role.¹²³ New stock listings were particularly impacted. Thomson Reuters' data indicated that Chi-X Europe had 20% of trading in the top 100 UK stocks, while LSE, a far older institution, had 67%. The Borsa Italiana had not been a solution to this critical problem.

Rolet oversaw the Baikal/Turquoise merger and technological acquisitions designed to modernize trading. He also reduced staffing in order to minimize operating costs and considered purchasing a majority stake in the clearing house operated by Fortis.¹²⁴ While this never came to pass, by 2014, the LSE allowed its customers to clear trades on EuroCCP.¹²⁵

Rapid changes in technology and finances pushed the LSE from reluctant participant in the new world order to cutting edge competitor.

C 2011 and Onwards

Throughout 2011, the LSE's newfound assertiveness and proactivity continued, as the Exchange sought to continue to diversify revenue and increase profit margins by seeking valuable new business partners. The LSE embarked on a strategy of spreading sources of revenue across every aspect of the trading cycle.

Merger fever though had not abated. In February 2011, the LSE announced a merger with the Canadian TMX, to create a combined entity with a 5 billion pound market capitalisation. The formidable Xavier Rolet was to head the group, with the TMX CEO to be president. Had the deal have gone ahead, the entity would have been the second largest exchange in the world.

¹²² Jeremy Grant, 'Rolet Speeds in to Push Change at LSE', *Financial Times* (London), 18 July 2009.

¹²³ Jeremy Grant, 'LSE Refreshes Baikal "Dark Pool"', above n 117.

¹²⁴ Lees, above n 36, 154.

¹²⁵ Phillip Stafford, 'LSE to Allow Customers to Clear Trades on EuroCCP', *Financial Times*, 21 May 2014.

Just weeks after the TMX merger was announced, Reuters reported rumours that the LSE was considering a takeover of NASDAQ. Questions to Xavier Rolet on whether a three-way merger might occur were deflected.¹²⁶ Ultimately, regulatory issues, including the reluctance of the LSE to be subject to the jurisdiction of the US regulator, the fearsome SEC, scuppered a NASDAQ merger.¹²⁷

On June 13, 2011, the Maple Group, a consortium of Canadian banks and pension funds, launched a cash and stock bid hoping to block the LSX/TMX merger. The LSE and TMX agreed to pay a special dividend, later that month, in order to sway shareholders away from the Maple rival bid. Unfortunately for the LSE, TMX shareholders did not back the merger, and subsequently, the Maple group deal was approved by Canadian authorities, giving birth to the TMX Group.

Although unsuccessful in its major merger attempt in 2011, the LSE did continue to pursue a course of smaller acquisitions in search of greater value added. The LSE purchased a remaining 50% stake in the FTSE 100 Index from Pearson.¹²⁸ The revenues produced by the FTSE 100 Index (GBP100 million in 2010) were the primary attraction.¹²⁹ The LSE also teamed up with a large syndicate of investment banks¹³⁰ to create the Turquoise Derivatives platform. This was to be a MTF for equity derivatives, listing securities from Norway, Russia and the UK.¹³¹

Diversification efforts continued in 2012, with the purchase of a 60% interest in LCH.Clearnet, the second largest clearer of bonds in the world. LCH.Clearnet also cleared across asset classes for a broad range of major international exchanges. Rolet asserted that the purchase of LCH.Clearnet was a transformative transaction which ‘sought to promote greater innovation, choice and competition in the listed derivatives market through this new-style open-access clearing model’.¹³² According to Rolet, the purchase built on the past success with Turquoise and the MTS Bond trading system acquired through the BI merger.¹³³

¹²⁶ Paritosh Bansal and Nadia Damouni, ‘London Stock Exchange Mulls NASDAQ Takeover: Report’, *Reuters* (New York), 7 March 2011.

¹²⁷ ‘Nasdaq Fails in Takeover Bid for London Stock Exchange’, above n 98.

¹²⁸ Lilly Vitorovich, ‘LSE to Buy Rest of FTSE’, *Wall Street Journal* (New York), 23 December 2011.

¹²⁹ *Ibid.*

¹³⁰ Including Barclays, Deutsche Bank, Goldman Sachs, JP Morgan, UBS and MF Global.

¹³¹ London Stock Exchange Group, *London Stock Exchange Derivatives Market* <<http://www.lseg.com/markets-products-and-services/our-markets/london-stock-exchange/derivatives-0>>

¹³² ‘LSE Wins Control of LCH.Clearnet’, *The Telegraph* (London), 02 April 2012 <<http://www.telegraph.co.uk/finance/markets/9180178/LSE-wins-control-of-LCH.Clearnet.html>>.

¹³³ *Ibid.*

Turquoise Derivatives disappeared in 2013 when the LSE bought it outright and renamed it ‘London Stock Exchange Derivatives Market’.¹³⁴ This move was partly designed to circumvent post-trade rules introduced in 2013 in the European Market Infrastructure Regulation (EMIR), which sought to impose higher costs on MTFs, because they are considered to be OTC.¹³⁵ By making Turquoise Derivatives part of a regulated market of a recognised investment exchange, London was able to improve market and capital usage.¹³⁶

In December 2014, LSE extended its geographic reach with its first major acquisition since 2011, Frank Russell, an American stock index and asset management business, for US\$2.7 billion.¹³⁷ The deal was touted to move the LSE further away from trading markets and the UK towards information services.¹³⁸ The Russell indices benchmark more than US\$5 trillion in assets, and include the ‘Russell 2000’, an index for small capitalisation American companies.¹³⁹

Diversification into clearing services, dark pools, derivatives and information services had produced the desired result, boosting LSE revenues by 50% to May 2014.¹⁴⁰ In early 2015, LSE was in talks with up to six bidders to sell Russell Investments, the asset management arm of the Frank Russell company. The LSE was not interested in that component of the business but had bid for the entire company to improve its chances of winning the initial bid.¹⁴¹

V CONCLUSION

The past 15 years have been a period of rapid adaptation by the LSE, from a stance of aloof independence to growth through acquisition and diversification. Once Clara Furse took the helm, market imperatives could not be denied; a merger was the right move, but on London’s terms.

¹³⁴ ‘London Stock Exchange to Acquire Turquoise Derivatives’, *FinExtra* (London), 5 July 2013 <<http://www.finextra.com/News/FullStory.aspx?newsitemid=24993>>.

¹³⁵ ‘EMIR Rules Prompt Turquoise Derivatives Reshuffle’, *The Trade* (online), 5 July 2013 <http://www.thetradenews.com/news/Trading_Venues/MTFs___ECNs/EMIR_rules_prompt_Turquoise_Derivatives_re_shuffle.aspx>.

¹³⁶ *Ibid.*

¹³⁷ Ian Walker and Josie Cox, ‘London Stock Exchange to Buy US Asset Manager Frank Russell for \$2.7 Billion’, *Wall Street Journal* (New York), 26 June 2014.

¹³⁸ *Ibid.*

¹³⁹ Arash Massoudi, Joseph Cotterill and Philip Stafford, ‘Bidders Circle Russell Investments Arm Auctioned by LSE’, *Financial Times* (London), 29 April 2015.

¹⁴⁰ *Ibid.*

¹⁴¹ *Ibid.*

But why did so much frenzied activity produce so little by way of tangible results? The early bids were associated with finely balanced incentives and disincentives, leading to impasse: corporate governance issues (in the form of shareholder relations), flawed merger strategies, a lack of synergies and simple under-valuations outweighed advantages. Regulatory complications and the LSE's perceived arrogance also contributed to proposed mergers unravelling. As time went on and the pace of internationalisation of the markets and technological change picked up, external factors played a role. In particular, exchanges sought partners bringing advanced technology and diversification to their business model.

The story of the LSE over the past 25 years is one of an institution caught in the midst of political, economic and technological change. Early on, adaptation, for a mutual association with such a long history of independence and such hidebound attitudes, was not easy. However, as compromise became necessary, and later on, unavoidable exposure to global change became a reality, the LSE was required to find its feet in the new world order. This took some time. The LSE came to realise it could not afford to continue missing opportunities to increase competitiveness, notwithstanding the regulatory and political issues involved. As ambitions of creating truly global exchanges grew, suitors became more savvy about how they approached the notoriously 'hard to get' LSE.¹⁴²

Moreover, the delay in merging straight away ultimately worked in the LSE's favour, if for no other reason than it let the exchange develop a strategy and a vision for the future that accommodated the changes occurring in the financial world. When it did finally make a move it was for the right reasons, and it escaped some of the regulatory issues that would have likely arisen had it taken up the offers of suitors like DB or NASDAQ. Increasingly short technological cycles and the advent of dark pools and ECNs forced the LSE to seek technological improvement and diversify its revenue streams. Recent times have even seen the Exchange finally enter the North American information market, with the acquisition and retention of Frank Russell Company's index business.

¹⁴² Lanchner, above n 76.

B.2 TORONTO – KEEPING IT CANADIAN^{*}

I INTRODUCTION

In 2011 and 2012, Canada witnessed a heated courtship focused around a group of Canadian exchanges, TMX Group. The London Stock Exchange Group plc (LSEG) wanted to merge with TMX Group in what was advertised as a merger of equals. However, nationalistic and business concerns prompted a consortium of Canadian businesses, Maple Group Acquisition Corp ('Maple'), to seek to take over TMX Group in competition with LSEG. Maple's pressure eventually paid off, with LSEG withdrawing its bid in June 2011. Maple then overcame various hurdles, and in 2012 took over TMX Group and some other Canadian businesses related to stock markets.

This paper examines the facts and consequences of these transactions. Part II provides context to the LSEG bid for TMX, identifying key trends and players in the Canadian market. It then examines the facts of the LSEG and Maple bids, ending with a discussion of some ramifications of Maple's success. Part III examines the issues posed by Canadian securities regulators which both Maple and LSEG had to face in their bids. Competition issues related to Maple's acquisition are examined in Part IV. Part V then examines other political issues surrounding the bids.

II THE FACTS

A Background

1 Initial Restructuring of Canadian Exchanges

On March 15, 1999, Canadian capital markets were restructured via a memorandum of agreement signed by executives of the Toronto, Alberta, Vancouver, and Montreal stock exchange.¹ This agreement made the Montreal Exchange (MX) a national derivatives exchange, while its equities trading was moved onto the Toronto, Alberta and Vancouver exchanges.² The Toronto Stock Exchange (TSX) became the home market for major companies, while smaller companies listed on the Vancouver and Alberta exchanges.³

^{*} The author would like to acknowledge, in particular, the assistance of Timothy Garvey with this chapter.

¹ Jean Campeau, Jean-Claude Cyr, and Pierre Rousseau, 'Proposed Restructuring of the Canadian Stock Exchanges' (Report, 5 May 1999) <<http://www.finances.gouv.qc.ca/documents/Autres/en/minoritaire.pdf>>.

² Ibid; Rhéal Séguin, 'How Quebec Played the Markets and Won', *The Globe and Mail* (Toronto), 28 April 2000.

³ Séguin, above n 2.

2 Demutualisation

The TSX and MX underwent demutualisation in 2000, becoming for-profit entities.⁴ Standard & Poor's assumed the management of the TSX 300 Composite Index in May 2002, and the name of that index was changed to the S&P/TSX Composite Index.⁵ In November 2002, the TSX became a public listed company.⁶ MX shares commenced public trading in March 2007.⁷

3 Domestic Consolidation

In May 2001, TSX acquired ownership over the Canadian Venture Exchange (CDNX), which meant that TSX had control over all Canadian equity trading.⁸ CDNX was renamed the TSX Venture Exchange in 2002.⁹ In 2004, TSX acquired full control over NGX, which was an electronic exchange for trading natural gas, and which also provided clearing and settlement services.¹⁰ In 2006, Scotia Capital's fixed income indices were purchased by one of TSX Group's subsidiaries, and TSX Group also acquired Shorcan Brokers Limited (SBL) through NGX.¹¹ SBL was a fixed income inter-dealer broker.¹² These acquisitions were part of TSX Group's strategy to diversify into different classes of assets, including fixed income.¹³

TSX merged with MX in 2008, creating TMX Group Inc. ('TMX Group').¹⁴ According to the then CEO of MX, Luc Bertrand, this merger brought 'together cash and derivatives trading for the first time.'¹⁵ The Canadian Derivatives Clearing Corporation (CDCC) was a wholly-owned subsidiary of MX, so TMX Group now controlled it also.¹⁶ CDCC provided clearing

⁴ Department of Finance Canada, *Information: Canada's Securities Industry* (January 2005), 5 <http://www.fin.gc.ca/activty/factsheets/cansec05_e.pdf>.

⁵ Ibid.

⁶ Ibid.

⁷ Reuters, *Montreal Exchange Profit Jumps with Trading Volume* (24 April 2007) <<http://uk.reuters.com/article/2007/04/24/montrealexchange-results-idUKN2440224920070424>>.

⁸ Department of Finance Canada, above n 4, 5.

⁹ Ibid.

¹⁰ NGX, *History* <http://www.ngx.com/?page_id=80>.

¹¹ IE Staff, 'TSX Group expands Canadian fixed income presence', *Investment Executive* (Canada), 25 October 2006; Jack W Plunkett, *Plunkett's Investment & Securities Industry Almanac: Investment & Securities Industry Market Research, Statistics, Trends & Leading Companies* (Plunkett Research, 2007).

¹² IE Staff, above n 11.

¹³ Ibid.

¹⁴ 'Briefly: TSX and MX Complete Merger', *Advisor.ca* (online), 1 May 2008 <<http://www.advisor.ca/news/industry-news/briefly-tsx-and-mx-complete-merger-23945>>; TMX Group Inc, *2008 Annual Report*, TMX, 62 <www.tmx.com/resource/en/77>.

¹⁵ 'Briefly: TSX and MX Complete Merger', above n 14.

¹⁶ Canadian Derivatives Clearing Corporation, *About CDCC* <http://www.cdcc.ca/about_index_en>.

and risk management services.¹⁷ Hence, various organisations were consolidated into the TMX Group.

4 Canadian Depository for Securities Limited

Incorporated in 1970, the Canadian Depository for Securities Limited (CDS) was set up ‘to create a centralized depository service and an electronic clearing and settlement system ...’¹⁸

A subsidiary of CDS – CDS Clearing and Depository Services Inc (CDSI) – owns and operates CDSX.¹⁹ CDSX was created in 2003, and provides various clearing and settlement services for both exchange and over-the-counter transactions.²⁰ In 2011, the services of CDS were used by 96 different dealers.²¹

5 Alpha

Alpha Trading Systems Inc and Alpha Trading Systems Limited Partnership (collectively, ‘Alpha’) operated as an alternative trading system (ATS),²² and was a rival to TMX.²³ Alpha’s ATS was launched in 2008, and provided competition to TMX Group through allowing investors to trade stocks listed on the TSX and TSX Venture Exchange.²⁴ Alpha was the second largest trading system within Canada just before the Maple transaction,²⁵ and accounted for 12% by volume (and 9% by value) of trading of S&P/TSX Composite Index companies in the six months before May 31, 2011.²⁶ Alpha also competed with TMX Group through a competing market data product which provided various trading information including stock quotes.²⁷ Before the Maple transaction, Alpha had applied to become a stock exchange, which would have allowed it to seek listings of its own.²⁸ This would have

¹⁷ Ibid.

¹⁸ TMX CDS, *History of CDS* <<http://www.cds.ca/newsroom/history>>.

¹⁹ Bank of Canada, *CDS Clearing and Depository Services Inc: Operator of CDSX*, Clearing and Settlement Systems <<http://www.bankofcanada.ca/core-functions/financial-system/clearing-and-settlement-systems/>>.

²⁰ Ibid; TMX CDS, above n 18.

²¹ Tim Kiladze, ‘Maple Firmly Promises To Keep CDS Fees Low’, *The Globe and Mail* (Toronto), 13 June 2011.

²² Maple Group Acquisition Corporation, *Proposed Acquisition of TMX Group, Alpha and CDS by Maple Group Acquisition Corporation* (3 October 2011), 1, 12, sch A (‘Proposed Acquisition’) <https://www.osc.gov.on.ca/en/Marketplaces_xxr-maple_20111007_pro-acquisition.htm>; Autorité des marchés financiers, *Notice of Public Consultation: Application Related to Proposed Acquisition by Maple Group Acquisition Corporation in Respect of TMX Group Inc and Proposed Subsequent Acquisitions of Alpha Trading Systems Limited Partnership, Alpha Trading Systems Inc and the Canadian Depository for Securities Limited* (7 October 2011) Acquisitions by Maple Group Acquisition Corporation <http://www.lautorite.qc.ca/files/pdf/consultations/bourses-chambres-oar/Maple_Consultation_ang.pdf> (‘Notice of Public Consultation’).

²³ Barbara Shecter, ‘TMX-Maple Deal Demanded Perfection’, *Financial Post* (Toronto), 31 January 2013.

²⁴ Boyd Erman, ‘Alpha Group Aims for Full Stock Exchange Status’, *The Globe and Mail* (Toronto), 22 April 2010.

²⁵ Boyd Erman, ‘TMX Shareholders Should Get Out of This Poker Game’, *The Globe and Mail* (Toronto), 13 June 2011.

²⁶ Maple Group Acquisition Corporation, *Proposed Acquisition*, above n 22; Autorité Des Marchés Financiers, above n 22.

²⁷ Boyd Erman, ‘Alpha Group Aims for Full Stock Exchange Status’, above n 24.

²⁸ Ibid.

provided further competition to TMX. However, after Maple's acquisition of Alpha, TMX Group 'decided not to pursue a listings strategy for Alpha.'²⁹

B The London Stock Exchange Proposal

By 2011, TMX Group's market share had been slowly being eroded since 2008.³⁰ The recent growth of several global exchanges had made it difficult for the TSX to advertise itself as an international marketplace.³¹ This was a key aspect of TSX's business strategy, since corporate listings were very profitable.³² Equity trading had decreased in importance in terms of generating revenue because of several reasons.³³ Firstly, high frequency trading and various electronic trading systems had driven down profits per trade.³⁴ Secondly, 30 to 35 percent of the Canadian market by volume had been taken by trading systems which rivalled TSX.³⁵ These circumstances surrounded the proposal for LSEG and TMX Group to undergo a 'merger of equals' which was announced on February 9, 2011.³⁶ The merger would not be a merger of any actual exchanges, but rather, according to TMX Group's CEO, Thomas Kloet, a 'pooling of ownership at the holding company level'.³⁷ LSEG's CEO, Xavier Rolet, stated the objective of the parties to the transaction: '[w]e are aiming at nothing less than becoming a true powerhouse in the global exchange business.'³⁸

The merged entity was to be jointly headquartered in Toronto and London,³⁹ and it would be the largest venue on the globe by number of total listings (more than 6,700 companies).⁴⁰ It would also be the largest venue for 'natural resources, mining, energy, and clean technology companies';⁴¹ and for 'international listings from emerging and growth markets'.⁴² The entity

²⁹ TMX Group Limited, *2012 Annual Report*, 15 <www.tmx.com/resource/en/65>.

³⁰ Tim Kiladze and Tara Perkins, 'TMX-LSE Merger Creates a New Global Player', *The Globe and Mail* (Toronto), 8 February 2011.

³¹ Ibid.

³² Ibid.

³³ Ibid.

³⁴ Ibid.

³⁵ Ibid.

³⁶ London Stock Exchange Group Plc and TMX Group Inc, 'London Stock Exchange Group Plc and TMX Group Inc Join Forces in Merger of Equals' (Press Release, 9 February 2011), 1 in sch A, *Form 51-102F3: Material Change Report* (9 February 2011) <www.tmx.com/resource/en/264> ('Press Release'); London Stock Exchange Group Plc and TMX Group Inc, *Merger Agreement: Execution Copy* (9 February 2011) TMX, 1 <www.tmx.com/resource/en/265> ('Merger Agreement').

³⁷ Financial Post Staff, 'TMX Fires Back at Banks on Merger', *Financial Post* (Toronto), 10 March 2011, quoting Thomas Kloet, 'Statement Responding to Open Letter from a Select Group of Financial Institutions' (Statement, 10 March 2011).

³⁸ London Stock Exchange Group Plc and TMX Group Inc, *Press Release*, above n 36.

³⁹ Ibid.

⁴⁰ Ibid.

⁴¹ Ibid.

⁴² Ibid.

would ‘offer an international gateway, leading global pools of capital formation and liquidity together with a unique portfolio of highly complementary markets, products, technologies and services.’⁴³ The merger was thought to be ‘strategically compelling’, and it would ‘create a more diversified business with greater scale, scope, reach and efficiencies, generating substantial benefits for all stakeholders’.⁴⁴ Its aim would include promoting capital raising and investment opportunities.⁴⁵ The entity would have 20 trading platforms or markets in Europe and North America, which would include trading in derivatives, equities, fixed income products and energy markets.⁴⁶ It would also possess various index, market data and global information businesses.⁴⁷ The merger was expected to result in cost synergies and increased revenue.⁴⁸ The increased revenue would come ‘from a variety of sources, including facilitation of cross-listings and admissions for customers (subject to regulatory approval), the wider availability of products and services via the Merged Group’s enhanced distribution and footprint, and the development of new products’.⁴⁹ Thomas Kloet saw benefits for both Canadians and Europeans in the transaction:

We are creating an international group with deep expertise, undeniable leadership in key sectors and the ability to compete and win on the global stage. Canadian customers will benefit from access to one of the world’s deepest capital pools while European issuers will have an effective gateway to North American financial markets. With some of the most valuable and respected brands in the exchange world, this merger will open new growth opportunities for each of our businesses and all of our stakeholders. This merger brings together talented market professionals across a wide geography, positioning the group for continued leadership in financial markets.⁵⁰

It was thought that the combined distribution networks of the groups would afford investors entry to cheaper, larger, and more liquid markets.⁵¹ Broadening the cost base of the two groups would also significantly foster the groups’ capacity to innovate rapidly and efficiently.⁵²

⁴³ Ibid.

⁴⁴ Ibid.

⁴⁵ Ibid.

⁴⁶ Ibid.

⁴⁷ Ibid.

⁴⁸ Ibid.

⁴⁹ Ibid.

⁵⁰ Ibid.

⁵¹ Ibid.

⁵² Kloet, above n 37, quoted in Financial Post Staff, above n 37.

There were further motivations for the deal from LSEG's perspective. First, it would protect LSEG from a potential takeover by a foreign predator.⁵³ Second, the sector was quickly consolidating,⁵⁴ and LSEG's shareholders thought the transatlantic merger with TMX Group was the best course of action.⁵⁵

1 *Balance: a 'Merger of Equals'*

The merged entity's board was to be comprised of fifteen directors, with seven nominated by TMX, and the other eight by the LSEG.⁵⁶ Its CEO was to be Xavier Rolet, LSEG's CEO.⁵⁷ However, the President and CFO of the entity were to come from TMX Group, and both were to be based in Toronto.⁵⁸ The Canadian-based President would 'manage the Merged Group's business units, as well as drive the implementation of strategy, mergers & acquisitions, partnerships and strategic ventures.'⁵⁹ Longer-term guarantees were given to entrench a perpetual Canadian representation on the merged entity's board, regardless of any future transaction.⁶⁰ Additionally, Canadian regulatory approval would be necessary for any future transaction causing a change of control.⁶¹

The merged entity's executive management and senior leadership were to be taken from both LSEG and TMX.⁶² Responsibility for the combined entity's businesses was not to be concentrated in one centre, but spread around various parts of the entity's geographic domain: Toronto would be responsible for primary markets (listings and other issuer services throughout the whole group), while responsibility for derivatives would be in Montreal, and for energy in Calgary.⁶³ London would remain a key international listings centre, and would be responsible for 'technology solutions, information services and post-trade services.'⁶⁴ Each market would remain subject to local regulators.⁶⁵ The exchanges would continue to operate under their pre-merger names.⁶⁶

⁵³ Helen Power, 'LSE Abandons Canadian Bid', *Business, The Times* (London), 30 June 2011, Edition 1 National Edition, 43.

⁵⁴ Ibid. For example, Deutsche Börse had recently joined forces with NYSE Euronext.

⁵⁵ Ibid.

⁵⁶ London Stock Exchange Group Plc and TMX Group Inc, *Press Release*, above n 36.

⁵⁷ Ibid.

⁵⁸ Ibid.

⁵⁹ Ibid.

⁶⁰ Kloet, above n 37, quoted in Financial Post Staff, above n 37; see London Stock Exchange Group Plc and TMX Group Inc, *Merger Agreement*, above n 36.

⁶¹ Kloet, above n 37, quoted in Financial Post Staff, above n 37.

⁶² London Stock Exchange Group Plc and TMX Group Inc, *Press Release*, above n 36.

⁶³ Ibid.

⁶⁴ Ibid.

⁶⁵ Ibid.

⁶⁶ Ibid.

There were strong political considerations relating to Canadian nationalism at play surrounding the LSEG proposal, which are discussed in Part V: ‘Political Problems’.

2 Mechanics of the Transaction

The proposal announced on February 9, 2011 would have meant 2.9963 LSEG ordinary shares per TMX share (the ‘exchange ratio’) would be given to TMX shareholders.⁶⁷ TMX Group shareholders resident in Canada could opt to receive the same number of shares in a Canadian subsidiary of LSEG, which could each be exchanged for an ordinary share of LSEG.⁶⁸ LSEG shareholders would retain majority ownership of the merged entity, but TMX shareholders would own 45% of the holding company,⁶⁹ LSEG (incorporated in the UK).⁷⁰ It would be listed on both the Toronto and London stock exchanges.⁷¹ After the transaction, shareholders would receive a regular dividend smaller than what they had received before it.⁷²

The merger required regulatory approval, approval by a court in Ontario, and also approval by TMX’s and LSEG’s shareholders.⁷³ TMX’s shareholders would be required to approve the merger by a minimum of two thirds of the votes cast at a special meeting.⁷⁴ It had been indicated that regulatory approvals would either be given unconditionally, or on satisfactory terms to both parties (considered reasonably).⁷⁵ Numerous undertakings would be given to various regulators if the merger were approved, including in areas such as: corporate governance; resource allocation; financial reporting; continuity of TSX management and core operations in Canada; compliance with undertakings to regulators such as the Autorité des marchés financiers (AMF), Alberta Securities Commission, and British Columbia Securities Commission; and access to information by the Ontario Securities Commission (OSC).⁷⁶ Securities regulatory issues are further discussed in Part IIIA: ‘Issues for the LSEG Proposal’.

LSEG was also required to obtain the approval of the Financial Services Authority (UK) and the UK Listing Authority for the relevant Prospectus and LSEG Circular.⁷⁷ LSEG was not

⁶⁷ Ibid.

⁶⁸ Ibid.

⁶⁹ Ibid.

⁷⁰ Ibid.

⁷¹ Ibid.

⁷² Boyd Erman, Grant Robertson and Tara Perkins, ‘Bidding War for TMX Heats Up’, *The Globe and Mail* (Toronto), 22 June 2011.

⁷³ London Stock Exchange Group Plc and TMX Group Inc, *Press Release*, above n 36.

⁷⁴ Ibid.

⁷⁵ Ibid.

⁷⁶ London Stock Exchange Group Plc and TMX Group Inc, *Merger Agreement*, above n 36.

⁷⁷ Ibid.

required by the *Merger Agreement* to subject itself to the US securities regulatory regime as a ‘reporting issuer’, however it retained the discretion to make ‘necessary or desirable’ ‘securities and other regulatory filings’ in any jurisdiction.⁷⁸

3 TMX and LSEG Boards Favoured the Proposal

The LSEG’s board thought the merger was ‘fair and reasonable’.⁷⁹ TMX Group’s board considered the merger to be ‘in the best interests of TMX’,⁸⁰ and unanimously approved the merger’s terms.⁸¹ Advice from Bank of America Merrill Lynch and BMO Capital Markets indicated the exchange ratio was financially fair to TMX’s shareholders.⁸²

4 LSEG Bid Made More Attractive to Canadian Investors

On June 22, 2011, LSEG and TMX Group announced a special dividend for TMX and LSEG shareholders, contingent on the merger’s completion.⁸³ LSEG shareholders would receive 84.1 pence for each share, while TMX Group shareholders would receive C\$4.00 for each share.⁸⁴ This dividend was intended to placate the large number of retail shareholders of TMX, who had been offered more consideration for their shares by Maple (discussed below in Part IIC: ‘Maple’s Proposal’).⁸⁵ It would be funded through increasing the merged entity’s total debt, though this would remain under half the debt with which TMX would be saddled under Maple’s offer.⁸⁶

The February proposal’s reduced regular dividend was a problem for some shareholders who sought income from their investments.⁸⁷ Investors globally had been seeking income-producing investments.⁸⁸ LSEG and TMX countered this on June 22 by announcing the pre-transaction dividend would be maintained if the merger took place.⁸⁹

5 Termination of the Merger Agreement

⁷⁸ Ibid.

⁷⁹ London Stock Exchange Group Plc and TMX Group Inc, *Press Release*, above n 36.

⁸⁰ Ibid.

⁸¹ Ibid.

⁸² Ibid.

⁸³ London Stock Exchange Group Plc, ‘London Stock Exchange Group Plc Special Dividend of 84.1 Pence per LSEG Share and C\$4.00 per TMX Group Share’ (Press Release, 22 June 2011) <<http://www.lseg.com/media-centre/news/corporate-press-releases/london-stock-exchange-group-plc-special-dividend-841>>.

⁸⁴ Ibid.

⁸⁵ Helen Power, ‘LSE Offers Sweetener To Secure Deal in Canada’, *Business, The Times* (London), 23 June 2011, Edition 1 National Edition, 45.

⁸⁶ Ibid.

⁸⁷ Erman, Robertson and Perkins, above n 72.

⁸⁸ Ibid.

⁸⁹ Ibid.

LSEG shareholders overwhelmingly supported the merger, however the situation was not the same in Canada.⁹⁰ Despite over half of TMX shareholder proxies supporting the merger, it was unlikely that the necessary affirmation of two thirds of TMX shareholders would be attained.⁹¹ The merger agreement was therefore terminated by the consent of the two groups on June 29, 2011.⁹² LSEG would receive \$10 million from TMX Group as an ‘expense fee’, and an extra \$29 million if the Maple deal (discussed in Part IIC: ‘Maple’s Proposal’) were accepted within a year and subsequently consummated.⁹³

C Maple’s Proposal

Opposition to the LSEG/TMX merger was strong within Canada. On March 9, 2011, several Canadian banking institutions indicated their opposition in an opinion piece in the *Financial Post*.⁹⁴ On May 13, 2011, Maple indicated it would make a counterbid to the LSEG proposal.⁹⁵ Maple was formed by an assortment of Canadian pension funds and banks,⁹⁶ and a significant motivation within the consortium was a concern that the LSEG proposal would be bad for Canada;⁹⁷ however profit-making motives were also present, particularly among the pension funds.⁹⁸ Luc Bertrand, a Maple spokesman, denied in June 2011 that Maple’s motivation concerned benefits to Canada, instead claiming that it was ‘the belief that we can build a better exchange and create more value for all concerned, including our respective shareholders and plan beneficiaries. In no way is this protectionist.’⁹⁹

The involvement of pension funds in the enterprise was crucial to prevent the perception that the banks merely wanted to reacquire that which they had lost through the TSX IPO in

⁹⁰ London Stock Exchange Group Plc, *Announcement re LSEG/TMX Group Merger* (Press Release, 29 June 2011) <<http://www.lseg.com/media-centre/news/corporate-press-releases/announcement-re-lsegtmx-group-merger>>.

⁹¹ Ibid.

⁹² Ibid.

⁹³ Ibid; Dana Flavelle, ‘Maple Bid Gathers Steam as TMX Merger Bites Dust; Canadian Group Likely To Benefit as Deal with London Called Off’, *Toronto Star* (Toronto), 30 June 2011.

⁹⁴ Financial Post Staff, ‘The Position That Has Divided Canada’s Banks’, *Financial Post* (Toronto), 9 March 2011. The institutions were TD Securities, CIBC World Markets, and National Bank Financial.

⁹⁵ Helen Power, ‘Canadians’ Bid for Toronto Bourse Threatens To Leave LSE Out in the Cold’, *Business, The Times* (London), 16 May 2011, Edition 1 National Edition, 37; Boyd Erman and Karen Howlett, ‘Banks, Pension Funds Offer to Buy TMX Group’, *The Globe and Mail* (Toronto), 14 May 2011.

⁹⁶ Erman and Howlett, ‘Banks, Pension Funds Offer to Buy TMX Group’, above n 95. These entities were the Toronto-Dominion Bank, Bank of Nova Scotia, National Bank of Canada, Canadian Imperial Bank of Commerce, Ontario Teachers’ Pension Plan, Canada Pension Plan Investment Board, Alberta Investment Management Co, Caisse de dépôt et placement du Quebec, and Fonds de solidarité des travailleurs du Quebec.

⁹⁷ Ibid.

⁹⁸ Boyd Erman and Karen Howlett, ‘New TMX Bid Pits Patriotism against Peril of Monopoly’, *The Globe and Mail* (Toronto), 15 May 2011.

⁹⁹ Luc Bertrand, ‘London-TMX Deal Won’t Give Canada Best, Most Competitive Exchange’, *The Globe and Mail* (online), 6 June 2011 <<http://www.theglobeandmail.com/globe-investor/london-tmx-deal-wont-give-canada-best-most-competitive-exchange/article582312/>>.

2002.¹⁰⁰ The involvement of the pension funds would ensure the group was run as a commercial undertaking, rather than as a ‘banks-only’ private club.¹⁰¹

Initially, directors in the TMX Group analysed Maple’s bid.¹⁰²

1 The Substance of the Initial Maple Bid

Maple’s offer was at a 22 percent premium above the LSEG’s.¹⁰³ Maple’s offer was a ‘part-cash, part-share bid’, which valued TMX Group at about \$48 per share, which was much higher than LSEG’s valuation of \$39.21 per share.¹⁰⁴ The consortium members could make this offer due to their combined power.¹⁰⁵ Maple also intended to maintain the pre-transaction dividend level.¹⁰⁶

A spokesman for Maple, Luc Bertrand, said Maple ‘believe[s] our offer constitutes a superior proposal under which shareholders would receive cash, plus the opportunity to continue to participate in the company’s ongoing growth.’¹⁰⁷ Under the Maple deal, Alpha and CDS would be merged into the TMX Group, which could stimulate growth and generate synergies.¹⁰⁸ The profit-making potential of this combination was a key incentive for some members of the Maple consortium.¹⁰⁹ The proposal would see the four Maple banks own 25 percent of TMX, the five pension funds own 35 percent, and the remaining 40 percent would be owned by the current shareholders of TMX (and able to be traded publicly).¹¹⁰ The consortium would give those current TMX shareholders \$33.52 in cash per share owned (without taking the shares).¹¹¹ No individual shareholder’s ownership would exceed 10 percent of the resulting entity.¹¹²

The Maple bid was non-binding, since it involved various conditions without specifying the means by which they would be satisfied.¹¹³ For example, regulatory approval was needed relating to the combination of Alpha, CDS, and TMX.¹¹⁴

¹⁰⁰ Erman and Howlett, ‘New TMX Bid Pits Patriotism against Peril of Monopoly’, above n 98.

¹⁰¹ Ibid.

¹⁰² Power, ‘Canadians’ Bid for Toronto Bourse Threatens To Leave LSE Out in the Cold’, above n 95.

¹⁰³ Ibid.

¹⁰⁴ Ibid.

¹⁰⁵ Erman and Howlett, ‘Banks, Pension Funds Offer to Buy TMX Group’, above n 95.

¹⁰⁶ Erman, Robertson and Perkins, above n 72.

¹⁰⁷ Power, ‘Canadians’ Bid for Toronto Bourse Threatens To Leave LSE Out in the Cold’, above n 95.

¹⁰⁸ Ibid; Erman and Howlett, ‘New TMX Bid Pits Patriotism against Peril of Monopoly’, above n 98.

¹⁰⁹ Erman and Howlett, ‘New TMX Bid Pits Patriotism against Peril of Monopoly’, above n 98.

¹¹⁰ Ibid.

¹¹¹ Ibid.

¹¹² Erman and Howlett, ‘Banks, Pension Funds Offer to Buy TMX Group’, above n 95.

¹¹³ Power, ‘Canadians’ Bid for Toronto Bourse Threatens To Leave LSE Out in the Cold’, above n 95.

2 TMX Group Board Rejects Maple Bid

On May 20, 2011, TMX Group's board rejected Maple's takeover bid, indicating that it still supported the LSEG proposal.¹¹⁵ TMX's board considered that Maple's proposal 'was too risky and vague.'¹¹⁶ In response, on May 25, 2011, Maple indicated it would take its offer directly to TMX Group shareholders, ignoring the board's support for the LSEG merger.¹¹⁷ On May 25, TMX and LSEG received approval from a court to have their shareholders vote on the LSEG proposal on 30 June, which Maple claimed forced its hand into making a hostile bid.¹¹⁸ A public relations war ensued.¹¹⁹ There were concerns that a failure of the LSEG proposal would leave the LSE itself vulnerable to being taken over (eg by Nasdaq, or by the Hong Kong or Singapore exchanges).¹²⁰

3 Maple Bid Goes Directly to Shareholders

For each TMX Group share, a shareholder could elect to receive either \$48 or one common share of Maple, subject to pro ration.¹²¹ The total cash payable could not exceed \$2.5 billion, and the total number of Maple shares issued could not exceed 22.5 million.¹²² 'On a fully prorated basis, each TMX Group share [would] be exchanged for \$33.52 in cash plus 0.3016 of a Maple share.'¹²³ The offer was contingent on the tender of two thirds or more of all outstanding TMX Group common shares.¹²⁴

Maple identified multiple reasons why the Maple offer would be beneficial to stakeholders. Some key reasons were: shareholders would receive greater cash consideration and value from the Maple offer;¹²⁵ Maple would maintain the dividend and an investment grade

¹¹⁴ Ibid.

¹¹⁵ 'Canadian Bid Rejected', *Business, The Times* (London), 21 May 2011, Edition 3 National Edition, 46.

¹¹⁶ Boyd Erman, 'Maple Group Goes Hostile after TMX Rejects Bid; Bank-Led Bidding Consortium Turns Up the Heat as TMX, LSE Set Shareholder Vote for June', *The Globe and Mail* (Toronto), 26 May 2011. TMX Group's board was concerned, inter alia, that the risk was too great for shareholders that the plan would not be approved by competition regulators.

¹¹⁷ Helen Power, 'Maple Group Steps Up Battle with LSE', *Sport, The Times* (London), 26 May 2011, Edition 2 National Edition, 55.

¹¹⁸ Boyd Erman, 'Maple Group Goes Hostile after TMX Rejects Bid; Bank-Led Bidding Consortium Turns Up the Heat as TMX, LSE Set Shareholder Vote for June', above n 116.

¹¹⁹ Shecter, 'TMX-Maple Deal Demanded Perfection', above n 23.

¹²⁰ Miles Costello and Helen Power, 'London Pours Scorn on Maple's Offer for Toronto Stock Exchange', *Business, The Times* (London), 27 May 2011, Edition 1, 62.

¹²¹ Maple Group Acquisition Corporation, *Maple Group Acquisition Corporation Announces Intention To Commence Offer To Acquire TMX Group* (25 May 2011) Ontario Teachers' Pension Plan <<http://www.otpp.com/news/article/-/article/22434>> ('*Intention to Commence Offer*').

¹²² Ibid.

¹²³ Ibid.

¹²⁴ Ibid.

¹²⁵ Ibid.

profile;¹²⁶ TMX Group would remain responsive to Canadian and international issuers' needs;¹²⁷ the strong Canadian regulatory and disclosure regime would remain applicable;¹²⁸ broker-dealers could profit from efficiencies resulting from the integration of trading and clearing for derivatives and cash;¹²⁹ Canada would benefit from continued investment in Canadian operational centres of excellence (eg Toronto, Montreal, and Calgary);¹³⁰ and TMX Group employees and management would benefit from greater opportunities in a bigger and better company.¹³¹ The combining of TMX, Alpha, and CDS would 'create an integrated trading and clearing exchange for equities, bonds, energy products and derivatives in both exchange-traded and over-the-counter ... markets.'¹³² This could lead to substantial synergies and growth which would benefit TMX Group and its shareholders, and also Canada's financial reputation.¹³³ Maple also considered its offer was better than the LSEG proposal 'because it was predicated upon expanding the Canadian group's business rather than stripping out costs'.¹³⁴ After consolidation with Alpha and CDS, the Maple entity might expand internationally.¹³⁵

Luc Bertrand also argued that Maple's involvement would facilitate technological investment by TMX, which could lead to efficiencies and better position the group for cross-listing agreements and acquisitions.¹³⁶ This could foster TMX's ability to engage in transactions internationally.¹³⁷

4 US Securities Law Interferes

Just before the bid was sent out to shareholders, with May's end approaching, Maple had to restructure its offer to comply with US securities law.¹³⁸ The problem arose because a significant number of US shareholders owned TMX stock.¹³⁹ In under a week, the offer was restructured to solve the problem: the transaction was to be completed in two steps.¹⁴⁰ The

¹²⁶ Ibid.

¹²⁷ Ibid.

¹²⁸ Ibid.

¹²⁹ Ibid.

¹³⁰ Ibid.

¹³¹ Ibid.

¹³² Ibid.

¹³³ Ibid.

¹³⁴ Alexandra Frean, 'Canadians Take Off Gloves in the Fight To Win Toronto Exchange; Local Consortium Tries To Trump LSE Offer', *Business, The Times* (London), 14 June 2011, Edition 1 National Edition, 41.

¹³⁵ Erman, Robertson and Perkins, above n 72.

¹³⁶ Bertrand, above n 99.

¹³⁷

¹³⁸ Shecter, 'TMX-Maple Deal Demanded Perfection', above n 23.

¹³⁹ Ibid.

¹⁴⁰ Ibid.

first step involved a partial takeover offer for money.¹⁴¹ The second step involved a subsequent share plan of arrangement.¹⁴² The offer under the second step was exempt from the *Securities Act of 1933* (US) under s 3(a)(10) of that Act.¹⁴³

5 Maple Begins Carrying Out its Offer

On June 13, 2011, Maple announced that it had begun to seek to acquire 70 percent of TMX Group's outstanding common shares.¹⁴⁴ This was part of an 'integrated acquisition transaction', consisting of two steps.¹⁴⁵ First, Maple would acquire the 70 percent of shares, each for \$48 in money.¹⁴⁶ Second, a plan of arrangement approved by a court would give shareholders (excluding Maple) 40 percent of Maple's shares in return for any TMX Group shares which they still possessed.¹⁴⁷ TMX shareholders were also urged to vote against the LSEG proposal, since Maple's transaction could not occur if the LSEG plan proceeded.¹⁴⁸

6 The Maple Consortium Grows

On June 12, 2011, Maple announced the addition of four new members to its consortium, increasing the perceived legitimacy of its cause.¹⁴⁹ These additions assisted in reducing concerns that the big banks in Maple would have excessive control over Canadian derivative and stock markets in the event of Maple's success.¹⁵⁰ The new membership meant that the four banks' stake in TMX Group if Maple's deal proceeded would fall from 25 percent to 21 percent.¹⁵¹ However, these additions were also the cause of some new problems. The new members had different motivations for joining the enterprise, potentially increasing the

¹⁴¹ Ibid.

¹⁴² Ibid.

¹⁴³ Maple Group Acquisition Corporation, *Maple Group Commences Offer To Acquire TMX Group as Part of an Integrated Transaction Valued at \$3.7 Billion* (13 June 2011) CNW <<http://www.newswire.ca/en/story/817119/maple-group-commences-offer-to-acquire-tmx-group-as-part-of-an-integrated-transaction-valued-at-3-7-billion>> ('*Commence Offer*'); *Securities Act of 1933*, 15 USC § 77c(a)(10) (2012): The section 3(a)(10) in this codification is identical to the s 3(a)(10) in force under the codification current in 2010. S 3(a)(10) exempted from the Act 'any security which is issued in exchange for one or more bona fide outstanding securities, claims or property interests, or partly in such exchange and partly for cash, where the terms and conditions of such issuance and exchange are approved, after a hearing upon the fairness of such terms and conditions at which all persons to whom it is proposed to issue securities in such exchange shall have the right to appear, by any court ...'

¹⁴⁴ Maple Group Acquisition Corporation, *Commence Offer*, above n 143.

¹⁴⁵ Ibid.

¹⁴⁶ Ibid.

¹⁴⁷ Ibid.

¹⁴⁸ Ibid.

¹⁴⁹ Boyd Erman, 'TMX Bidders Bulk Up, but a Balancing Act; Addition of Desjardins, Manulife and Two Securities Firms Will Help Consortium Counter Perception the Banks Have Too Much Control', *The Globe and Mail* (Toronto), 13 June 2011. The four new members were: Desjardins Group (Canada's biggest financial cooperative), Manulife Financial Corp (the largest insurer in Canada), GMP Capital Inc (a securities firm), and Dundee Securities Corp (also a securities firm).

¹⁵⁰ Ibid.

¹⁵¹ Ibid.

difficulty in reaching collective decisions.¹⁵² For example, Desjardins introduced the novel motivation that Maple might provide a better result for Quebec, while Dundee and GMP considered Maple's deal was more beneficial for smaller businesses.¹⁵³ Problems could also be exacerbated through the fact that some consortium members, predominantly the banks, had ownership stakes in Alpha and CDS, and so would like the prices paid by Maple for those entities to be higher.¹⁵⁴ The addition of more members with interests in keeping the prices lower could further complicate internal consortium negotiations.¹⁵⁵ However, Maple intended to create a committee comprised of independent directors to oversee those acquisitions and ensure that the consideration given would be fair for shareholders, and a binding arbitration process was available if the parties could not agree.¹⁵⁶ This would likely mitigate potential conflicts within Maple in this area.

7 Suggestions That Maple Would Be Approved by the Competition Regulator

There were numerous serious competition issues raised by the Maple proposal (these are discussed in Part D: 'Competition Concerns'). On June 16, 2011, it was revealed that Maple's lawyers were advising that the Maple deal would not be blocked on competition grounds by the regulator.¹⁵⁷ Maple also allegedly had a plan to satisfy the national Competition Bureau.¹⁵⁸ This information reported to the public could have gone some way towards assuaging various peoples' concerns about the Maple transaction relating to the risk that it would not be approved.

8 Maple Sweetens Its Bid

In response to the sweetening of LSEG's bid, Maple surpassed the rival offer on June 22, 2011 by offering TMX shareholders who voted in favour of Maple's bid \$50 per share (increased from \$48).¹⁵⁹ It also increased the component of its offer in cash to \$40 per share (increased by \$6.40).¹⁶⁰ The consortium's members also agreed to provide additional equity,

¹⁵² Ibid.

¹⁵³ Ibid.

¹⁵⁴ Ibid.

¹⁵⁵ Ibid.

¹⁵⁶ Maple Group Acquisition Corporation, *Commence Offer*, above n 143.

¹⁵⁷ Helen Power, 'Canadians Claim Backing of Watchdog in Battle with the LSE for Toronto Exchange', *Business, The Times* (London), 17 June 2011, Edition 2 National Edition, 62.

¹⁵⁸ Ibid.

¹⁵⁹ Erman, Robertson and Perkins, above n 72; Helen Power and Chris Johnston, 'Maple Puts LSE on the Back Foot', *Business, The Times* (London), 24 June 2011, Edition 1 Scotland, 51; Shecter, 'TMX-Maple Deal Demanded Perfection', above n 23.

¹⁶⁰ Shecter, 'TMX-Maple Deal Demanded Perfection', above n 23.

which gave Maple the ability to acquire an additional ten percent of TMX's shares (up to 80 percent).¹⁶¹

9 Lead-up to 30 June Vote on LSEG Deal

Some investors and banks which were not part of the Maple consortium supported the LSEG proposal on June 27, 2011 through an open letter.¹⁶² Heads of eleven financial institutions said the LSEG offer preserved competition and Canadian regulatory paramountcy, and promoted Canadian executive management.¹⁶³ They also criticised the Maple deal as generating a national monopoly and conflicts of interest.¹⁶⁴ However, this intervention was not enough to save the LSEG deal, as it was abandoned on June 29, 2011,¹⁶⁵ leaving Maple to pursue its prey alone.

10 Maple's Deal after the LSEG's Failure

On July 21, 2011, with the LSEG bid having failed, TMX's board authorised discussions between TMX's advisors and management and Maple concerning Maple's offer.¹⁶⁶ On October 30, 2011, TMX's board announced that it unanimously supported the Maple deal and advised TMX shareholders to accept it.¹⁶⁷ The accepted deal had the same structure and offer price as Maple's amended offer on June 22, 2011.¹⁶⁸ The TMX board was influenced by various considerations, including:¹⁶⁹ the offer provided a unique opportunity to form an integrated group providing exchange and clearing services;¹⁷⁰ the integration of CDS into the group would lead to cost savings and generate capital efficiencies, as well as increasing TMX's capacity to provide clearing solutions for over-the-counter trades in Canadian markets;¹⁷¹ the combination of Alpha, CDS and TMX would make the group more internationally competitive, positioning it well for growth in the global exchange industry which had become more competitive and consolidated;¹⁷² and the combination of those three

¹⁶¹ Erman, Robertson and Perkins, above n 72.

¹⁶² Helen Power, 'Rival Bidder Turns Up Pressure on the LSE', *Business, The Times* (London), 28 June 2011, Edition 1 National Edition, 34.

¹⁶³ Ibid.

¹⁶⁴ Ibid.

¹⁶⁵ Power, 'LSE Abandons Canadian Bid', above n 53.

¹⁶⁶ TMX Group Inc, 'TMX Group Board of Directors Authorizes Discussions with Maple Group' (News Release, 21 July 2011) Bloomberg <<http://www.bloomberg.com/apps/news?pid=newsarchive&sid=agijFlZcE3oc>>.

¹⁶⁷ TMX Group Inc and Maple Group Acquisition Corporation, 'TMX Group and Maple Group Enter into Support Agreement' (30 October 2011) CNW <<http://www.newswire.ca/en/story/868049/tmx-group-and-maple-group-enter-into-support-agreement>>.

¹⁶⁸ Ibid.

¹⁶⁹ Ibid.

¹⁷⁰ Ibid.

¹⁷¹ Ibid.

¹⁷² Ibid.

would increase the group's capacity for joint ventures and international acquisitions.¹⁷³ The board also considered matters relating to corporate governance in the Maple agreement, including the appointment of particular numbers of independent directors and directors of the old TMX board to the resulting entity's board.¹⁷⁴

It was confirmed on July 4, 2012 that Maple would obtain a No Action Letter for its transaction from the Competition Bureau (discussed further in Part D: 'Competition Concerns').¹⁷⁵ The final regulatory hurdles to the transaction were cleared on July 11, 2012 when the Alberta Securities Commission and the British Columbia Securities Commission approved the deal.¹⁷⁶ The Ontario Securities Commission, which was the TSX's primary regulator, had also recently approved the deal.¹⁷⁷ Securities regulation issues for the Maple transaction are further discussed in Part IIIB: 'Issues for the Maple Proposal'.

11 *Maple Finishes the Deal*

Maple and TMX announced on July 31, 2012 that all the conditions for Maple to proceed with its offer had been satisfied, and that all TMX shares deposited as part of the offer had been accepted by Maple.¹⁷⁸ On August 1, 2012, Maple announced that it had acquired CDS and Alpha.¹⁷⁹ On August 10, 2012, 95.4% of TMX Group shares had been tendered to Maple.¹⁸⁰ Following the terms of its offer, Maple acquired 80% and the remainder would be returned to TMX shareholders.¹⁸¹ Maple was to pay \$50 per share acquired.¹⁸² On the same day, Maple's name was formally changed to TMX Group Limited ('TMX Ltd').¹⁸³

¹⁷³ Ibid.

¹⁷⁴ Ibid.

¹⁷⁵ Competition Bureau, *Competition Bureau Completes Review of Proposed Maple-TMX Transaction* (4 July 2012) Competition Bureau <<http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03480.html>>.

¹⁷⁶ Boyd Erman, 'Maple Bid for TMX Clears Last Regulatory Hurdles', *The Globe and Mail* (Toronto), 11 July 2012.

¹⁷⁷ Ibid.

¹⁷⁸ Maple Group Acquisition Corporation, 'Maple Announces Completion of Acquisitions of CDS and Alpha' (News Release, 1 August 2012) TMX <<http://www.cds.ca/newsroom?id=149&year=2012>>.

¹⁷⁹ Ibid.

¹⁸⁰ TMX Group Inc and TMX Group Limited, 'Maple and TMX Group Announce Completion of Offer' (10 August 2012) PR Newswire <<http://www.prnewswire.com/news-releases/maple-and-tmx-group-announce-completion-of-offer-165793096.html>>.

¹⁸¹ Ibid.

¹⁸² Ibid; John Shmuel, 'TMX Group Shares Take 10% Plunge; CIBC Analyst Cites Debt Load as Main Hurdle', *Financial Post Investing, National Post's Financial Post & FP Investing* (Toronto), 14 August 2012, FP6.

¹⁸³ TMX Group Inc and TMX Group Limited, 'Maple and TMX Group Announce Completion of Offer', above n 180.

TMX Group's shareholders approved the Maple arrangement on September 12, 2012.¹⁸⁴ On September 13, 2012, TMX Group announced that the Ontario Superior Court of Justice had approved the transaction involving TMX Group and TMX Ltd.¹⁸⁵ The following day, the two companies announced that the second step of the Maple transaction had been completed.¹⁸⁶ TMX Ltd had acquired all outstanding TMX Group shares (except those held by TMX Ltd), exchanging each share for one share in TMX Ltd.¹⁸⁷ TMX Ltd then owned all TMX Group shares.¹⁸⁸ The takeover was complete.

D The Aftermath of the Maple Transaction

The boards of Maple, TMX Group and TMX's principal operating subsidiaries were constituted by the same people in July 2012.¹⁸⁹

Just after its acquisition of Alpha and CDS, the TMX Group juggernaut accounted for 90 percent of Canadian equities trading.¹⁹⁰ In the first full quarter after Maple took control of TMX Group, TMX earned 95 cents per share (excluding one off purchases pertaining to the acquisition), while analysts had expected the figure to be 73 cents per share.¹⁹¹

There were around 1300 employees of TMX Group by the end of September 2012.¹⁹² However, the group intended to remove 100 positions over the 12 months following November 2012 as part of the process of integrating Alpha and CDS into the wider corporate group.¹⁹³ Corporate support functions were in the firing line, and their consolidation over the various corporations would deliver efficiencies in operation and monetary savings.¹⁹⁴ Hence, at least some of the promised synergies appeared to be eventuating.

¹⁸⁴ TMX Group Inc and TMX Group Limited, 'TMX Group Inc and TMX Group Limited Announce Completion of Subsequent Arrangement' (News Release, 14 September 2012) TMX <www.tmx.com/resource/en/319>.

¹⁸⁵ TMX Group Inc, *TMX Group Inc Obtains Court Approval for Arrangement* (13 September 2012) TMX <www.tmx.com/resource/en/317>.

¹⁸⁶ TMX Group Inc and TMX Group Limited, 'TMX Group Inc and TMX Group Limited Announce Completion of Subsequent Arrangement', above n 184.

¹⁸⁷ Ibid.

¹⁸⁸ Ibid.

¹⁸⁹ Maple Group Acquisition Corporation and TMX Group Inc, 'Maple and TMX Group Announce Take Up under Maple Offer; All Conditions to Maple Offer Have Been Satisfied' (31 July 2012) CNW <<http://www.newswire.ca/en/story/1014893/maple-and-tmx-group-announce-take-up-under-maple-offer-all-conditions-to-maple-offer-have-been-satisfied>>.

¹⁹⁰ Shmuel, above n 182.

¹⁹¹ Alastair Sharp, 'TMX Wraps Up Takeover Year with Profit; Operator of the Toronto Exchange Posts Better-Than-Expected Earnings of \$32.8-Million in Fourth Quarter', *The Globe and Mail* (Toronto), 7 February 2013, B5.

¹⁹² David Friend, 'Stock Exchange Group To Cut 100 Positions', *Toronto Star* (Toronto), 10 November 2012, S16.

¹⁹³ Ibid.

¹⁹⁴ Ibid.

In early 2013, TMX management indicated that foreign acquisitions by the group were unlikely, despite having previously discussed the possibility.¹⁹⁵ Management indicated that the main focus would be on the integration of businesses within the group, such as Alpha and CDS.¹⁹⁶

Before the Maple transaction, banks which were TMX's biggest customers were in the process of creating Alpha, a competitor to TMX, because they perceived TMX to be overcharging and under delivering.¹⁹⁷ Because of the Maple deal, TMX Group acquired Alpha, and the banks were back on side.¹⁹⁸ With the danger posed by Alpha neutralised and other areas within the TMX group expanding (such as the clearing business), it was easier for TMX to cope with the fact that its traditional business – trading in stocks – had been declining.¹⁹⁹

As of June 2013, barriers to entry to the markets for clearing and settlement were high.²⁰⁰ This decreased the likelihood that TMX Ltd would face new competition in those markets.

III SECURITIES REGULATION ISSUES

A Issues for the LSEG Proposal

LSEG had to persuade provincial securities regulators that the proposed merger would not harm the regulation of Canadian markets or 'cause a hollowing out of the Canadian financial sector.'²⁰¹ No single entity could own over 10 percent of TMX unless approved by the Quebec and Ontario securities regulators.²⁰² The core issues which may have concerned the regulators were likely to have been about the governance of the merged entity, and why TMX, and therefore Canada, was perceived to be the minor partner in a deal supposed to be a merger of equals.²⁰³

¹⁹⁵ Sharp, above n 191.

¹⁹⁶ Ibid.

¹⁹⁷ Boyd Erman, 'On Bay Street, but Not of It; Tom Kloet, Chief Executive Officer, TMX Group Inc Two Years Ago Today, the Boss of Canada's Stock Exchange Announced a Plan To Merge the Company with Its London Counterpart. The Deal Was Ultimately Thwarted, but the Tumultuous Period Stands to Reshape the Way Investors Do Business in Canadian Markets', *The Globe and Mail* (Toronto), 9 February 2013, B3.

¹⁹⁸ Ibid.

¹⁹⁹ Ibid.

²⁰⁰ Barbara Shecter, 'Is There Room for Two on Bay Street?; Aequitas Seeking Regulatory Approval This Year', *National Post* (Canada), 26 June 2013, FP1.

²⁰¹ Erman, 'TMX Shareholders Should Get Out of This Poker Game', above n 25.

²⁰² McFarland, 'OSC Sets July Dates for TMX Hearings', *The Globe and Mail* (Toronto), 15 June 2011.

²⁰³ Erman, 'TMX Shareholders Should Get Out of This Poker Game', above n 25.

The OSC, one of the provincial regulators which needed to approve the LSEG proposal for it to proceed, indicated that ‘the public interest’ was the deciding issue.²⁰⁴ The chairman of the OSC had previously indicated that relevant considerations included corporate governance, market integrity, and share ownership issues.²⁰⁵

B Issues for the Maple Proposal

For the Maple proposal, four provincial securities regulators – those in Ontario, British Columbia, Alberta, and Quebec – engaged in very thorough analysis.²⁰⁶ These regulators each had different market sector and geographic concerns.²⁰⁷ In the end, the regulators required concessions concerning controls on governance and conflicts of interest.²⁰⁸ Two large Canadian banks – Royal Bank of Canada and Bank of Montreal – were not members of the Maple group, which helped to assuage the concerns of regulators and thus permit the proposal to proceed.²⁰⁹

1 Autorité des Marchés Financiers Approval

The Quebec regulator approved most of the Maple deal (other than recognising Maple, CDS, and CDSI as clearing houses) on May 3, 2012.²¹⁰ It imposed various conditions,²¹¹ including relating to share ownership and corporate governance.²¹² Maple gave undertakings, including to ‘maintain and continue to develop Montréal as a centre of excellence in derivatives’.²¹³

AMF recognised Maple, CDS, and CDSI as clearing houses on July 4, 2012, subject to conditions.²¹⁴

2 Ontario Securities Commission Recognition Orders

The OSC issued orders on July 4, 2012 recognizing Maple, TMX, and Alpha as exchanges and approved the Maple transaction, subject to various conditions.²¹⁵ The particular focus of

²⁰⁴ McFarland, above n 202.

²⁰⁵ Ibid.

²⁰⁶ Shecter, ‘TMX-Maple Deal Demanded Perfection’, above n 23.

²⁰⁷ Ibid.

²⁰⁸ Ibid.

²⁰⁹ Ibid.

²¹⁰ Autorité des marchés financiers, ‘Proposed Acquisition of TMX Group by Maple Group Acquisition Corporation - AMF Issues Certain Decisions and Launches Consultation on CDS’ (News Release, 3 May 2012) <http://www.lautorite.qc.ca/en/press-releases-2012-autre.html_2012_decision-maple-2012-05-03.html>; Autorité des marchés financiers, *Notice of Public Consultation*, above n 22.

²¹¹ Autorité des marchés financiers, *Notice of Public Consultation*, above n 22.

²¹² Ibid.

²¹³ Ibid.

²¹⁴ Autorité des marchés financiers, ‘Proposed Acquisition of TMX Group Inc by Maple Group Acquisition Corporation - AMF Issues Certain Decisions and Launches Consultation on CDS’, above n 210.

the Commission was on the ‘public interest’.²¹⁶ The Commission would enhance its oversight of Maple in light of the transaction ‘which could concentrate risk in Maple, and the significant amount of conflicts that could result’.²¹⁷

In relation to the exchanges, the OSC imposed conditions including a prohibition on the provision of discounts or rebates to a particular class of market users without Commission approval, and an absolute prohibition on such discounts or rebates to any particular market user.²¹⁸ There could be no fee arrangement which required the use of a Maple clearing agency for the continued use of a Maple exchange.²¹⁹ The Commission also imposed corporate governance requirements and required ‘that the choice of listing venues in the course of underwriting activities must be made without regard to ownership interests of a Maple dealer in a Maple recognized exchange.’²²⁰

To promote competition in the clearing, settlement and depository services markets, CDS ‘rules and any arrangements between CDS and its participants [must] not prohibit, limit or impede the ability of participants to choose which entity it wishes to engage to perform the post-trade clearing, settlement or depository services.’²²¹ Additionally, they may not impede

²¹⁵ Ontario Securities Commission, *Maple Group Acquisition Corporation: Notice of Commission Approval* (4 July 2012) in *Maple Group Acquisition Corporation: Notice of Commission Approval and Recognition Orders* (4 July 2012) <https://www.osc.gov.on.ca/en/Marketplaces_xxr-maple_20120704_recognition-orders.htm> (‘Notice of Commission Approval’); Ontario Securities Commission, ‘OSC Publishes Recognition Orders for Maple Transaction’ (News Release, 4 July 2012) <https://www.osc.gov.on.ca/en/NewsEvents_nr_20120704_osc-maple-orders.htm>.

²¹⁶ Ontario Securities Commission, ‘OSC Publishes Recognition Orders for Maple Transaction’, above n 215.

²¹⁷ Ontario Securities Commission, *Notice of Commission Approval*, above n 215.

²¹⁸ Ibid; Ontario Securities Commission, *In the Matter of the Securities Act, RSO 1990, Chapter S5, as Amended (Act) and in the Matter of Maple Group Acquisition Corporation and TMX Group Inc and TSX Inc and Alpha Trading Systems Limited Partnership Alpha Trading Systems Inc Alpha Market Services Inc and Alpha Exchange Inc and in the Matter of Alberta Investment Management Corporation Caisse De Dépôt Et Placement Du Québec Canada Pension Plan Investment Board CIBC World Markets Inc Desjardins Financial Corporation Dundee Capital Markets Inc Fonds De Solidarité Des Travailleurs Du Québec (FTQ) the Manufacturers Life Insurance Company National Bank Financial & Co Inc Ontario Teachers' Pension Plan Board Scotia Capital Inc and TD Securities Inc Order (Sections 21, 21.11 and 144 of the Act)* (4 July 2012) in *Maple Group Acquisition Corporation Notice of Commission Approval and Recognition Orders* (4 July 2012) <https://www.osc.gov.on.ca/en/Marketplaces_xxr-maple_20120704_recognition-orders.htm>.

²¹⁹ Ibid.

²²⁰ Ibid; Ontario Securities Commission, *In the Matter of the Securities Act, RSO 1990, Chapter S5, as Amended (Act) and in the Matter of Maple Group Acquisition Corporation and TMX Group Inc and TSX Inc and Alpha Trading Systems Limited Partnership Alpha Trading Systems Inc Alpha Market Services Inc and Alpha Exchange Inc and in the Matter of Alberta Investment Management Corporation Caisse De Dépôt Et Placement Du Québec Canada Pension Plan Investment Board CIBC World Markets Inc Desjardins Financial Corporation Dundee Capital Markets Inc Fonds De Solidarité Des Travailleurs Du Québec (FTQ) the Manufacturers Life Insurance Company National Bank Financial & Co Inc Ontario Teachers' Pension Plan Board Scotia Capital Inc and TD Securities Inc Order (Sections 21, 21.11 and 144 of the Act)* (4 July 2012) in *Maple Group Acquisition Corporation Notice of Commission Approval and Recognition Orders* (4 July 2012) <https://www.osc.gov.on.ca/en/Marketplaces_xxr-maple_20120704_recognition-orders.htm>.

²²¹ Ontario Securities Commission, *Notice of Commission Approval*, above n 215.

‘a third party service provider in the provision of its services.’²²² The Commission also imposed other conditions, including in relation to fees and transparency.²²³

IV COMPETITION CONCERNS

Once the LSE proposal had died, the Maple group required the approval of competition regulators to proceed, including the federal Competition Bureau.²²⁴ The federal Commissioner of Competition, Melanie Aitken, had said in November 2011 that she had ‘serious concerns’ regarding the deal.²²⁵ The main trouble spots for competition concerns were the Canadian equities market, the area of market data sales, and the area of listings.

A Competition Concerns

Maple had to satisfy the Competition Bureau that its creation of a near-monopoly on services such as stock trading would not harm businesses or investors.²²⁶ Melanie Aitken, the Competition Commissioner, had recently adopted a very strong stance against monopolies.²²⁷ Maple’s proposal would result in some of Canada’s biggest pension funds and banks, which already owned Alpha, becoming 80 percent owners of TMX Group and the exchanges which it owned (including the TSX, the Montreal derivatives exchange, and the Alberta venture exchange),²²⁸ and the entity resulting from the transaction would deal with over 80 percent of the Canadian equities market.²²⁹

A further competition concern arose from the competition between Alpha and TMX in the area of market data sales.²³⁰ Alpha had an estimated market share of 10 to 15 percent in this market, and was probably TMX’s largest competitor.²³¹ The combination of the largest and

²²² Ibid.

²²³ Ibid; Ontario Securities Commission, *In the Matter of the Securities Act, RSO 1990, Chapter S5, as Amended ("Act") and in the Matter of the Canadian Depository for Securities Limited and CDS Clearing and Depository Services Inc Order (Sections 21.2 and 144 of the Act)* (4 July 2012) in *Maple Group Acquisition Corporation: Notice of Commission Approval and Recognition Orders* (4 July 2012) <https://www.osc.gov.on.ca/en/Marketplaces_xxr-maple_20120704_recognition-orders.htm>.

²²⁴ Boyd Erman, ‘LSE “Reviewing” Its Bid for TMX Group’, *The Globe and Mail* (Toronto), 16 June 2011; Kiladze, ‘Maple Group’s Next Stop in Bid for TMX Group: Ottawa’, *The Globe and Mail* (Toronto), 29 June 2011.

²²⁵ Shecter, ‘TMX-Maple Deal Demanded Perfection’, above n 23.

²²⁶ Kiladze, ‘Maple Group’s Next Stop in Bid for TMX Group: Ottawa’, above n 224; Erman, ‘TMX Shareholders Should Get Out of This Poker Game’, above n 25.

²²⁷ Ibid.

²²⁸ Flavelle, above n 93.

²²⁹ Kiladze, ‘Maple Group’s Next Stop in Bid for TMX Group: Ottawa’, above n 224.

²³⁰ Erman, ‘TMX Shareholders Should Get Out of This Poker Game’, above n 25.

²³¹ Ibid.

second-largest providers of these sales hence had the potential to raise serious competition issues.²³²

The final relevant consideration was that Alpha sought to compete with TMX in the area of listings in the future, however merging the two would prevent such competition.²³³

B The Arguments

Maple contended that the Commission should look at the broader international market when considering the transaction's competition ramifications in the area of stock listings.²³⁴ It argued that international competition in that area was sufficient, and also that if the TMX were strengthened it could acquire other exchanges.²³⁵

Maple contended that the Competition Bureau should focus on the entire North American stock trading market, rather than only on the Canadian market, when considering market share.²³⁶ Less than 50 percent of the trading of stocks on the S&P/TSX composite index was via the services of Alpha or the TSX, since much of it occurred in the United States.²³⁷ However, fewer than 10 percent of listed companies in Canada were on the S&P/TSX composite index, and less were cross-listed and able to be traded in the United States.²³⁸ Most listed companies in Canada could only be traded on a Canadian stock exchange.²³⁹ The combined market share of TMX and Alpha for that sort of securities was around 85 percent.²⁴⁰ This indicates that the influence which the broader North American market may have been able to have on potential anticompetitive activities by the merged entity could be small. Nevertheless, the spokesman of the Maple Group, Luc Bertrand, argued that trading volume in some large Canadian corporations could head south to the United States in the event of US fees being lower than those of TMX, which could constrain TMX's capacity to charge higher fees.²⁴¹

Mr Bertrand also argued that alternative trading platforms *within* Canada, including Omega ATS and Chi-X, would constrain the merged entity from increasing fees by taking trades

²³² Ibid.

²³³ Ibid.

²³⁴ Flavelle, above n 93.

²³⁵ Ibid.

²³⁶ Ibid.

²³⁷ Erman, 'TMX Shareholders Should Get Out of This Poker Game', above n 25.

²³⁸ Ibid.

²³⁹ Ibid.

²⁴⁰ Ibid.

²⁴¹ Tara Perkins, 'Patriot Games: Why Aimco Backs Maple's TMX Bid', *The Globe and Mail* (Toronto), 4 July 2011.

from it through lower rates.²⁴² The only area in which TMX and Alpha competed with each other was in equities trading.²⁴³ Omega and Chi-X, as well Pure and other alternative trading systems within Canada, offered competitive alternatives for equities trading.²⁴⁴ These competitors possessed the resources to deal with trading volumes far exceeding those with which Alpha actually dealt.²⁴⁵ This ability, coupled with the fact that dealers were compelled by Canadian securities regulations to make trades via whichever system provided the optimal price, meant that there would still be significant competition in equities trading.²⁴⁶

Mr Bertrand also identified that the banks within Maple were large customers of the TMX Group, and hence would benefit from lower trading fees.²⁴⁷ They therefore would not have an interest in seeking to increase fees.²⁴⁸

A separate argument from Maple was that there were low barriers to entry in the stock trading market, and that other trading systems had plenty of capacity to expand into the market.²⁴⁹ Hence, these would constrain Maple from raising prices even with its massive market share.²⁵⁰

Finally, in an attempt to assuage regulatory concerns about competition, Maple indicated that if it were permitted to merge CDS Inc with TMX Group, it would not increase costs.²⁵¹

C Competition Bureau's Judgment

The Commissioner of Competition, Melanie Aitken, released a statement on July 4, 2012 confirming that the Competition Bureau would issue a No Action Letter to Maple Group regarding Maple's proposed acquisitions of TMX Group, Alpha, and CDS.²⁵² The Bureau had originally been seriously concerned primarily with respect to equities trading and post-trade services (such as settlement, clearing and depository services).²⁵³ However, the views of the Bureau changed in light of recognition orders made on the same day by the Ontario

²⁴² Ibid.

²⁴³ Bertrand, above n 99.

²⁴⁴ Ibid.

²⁴⁵ Ibid.

²⁴⁶ Ibid.

²⁴⁷ Ibid.

²⁴⁸ Ibid.

²⁴⁹ Boyd Erman and Karen Howlett, 'Shareholders Reject Proposed Merger of TMX and LSE', *The Globe and Mail* (Toronto), 29 June 2011.

²⁵⁰ Ibid.

²⁵¹ Ibid.

²⁵² Competition Bureau, above n 175.

²⁵³ Ibid.

Securities Commission (see Part IIIB: ‘Issues for the Maple Proposal’).²⁵⁴ The Bureau had made submissions to the OSC regarding potential effects on competition from the proposed transactions.²⁵⁵ According to Commissioner Aitken, ‘the OSC’s final recognition orders materially change the regulatory environment sufficient[ly] to substantially mitigate the Bureau’s competition concerns.’²⁵⁶ As a result, the Bureau decided not to challenge the transactions in the Competition Tribunal.²⁵⁷

V POLITICAL PROBLEMS

Strong political considerations were at play in Canada surrounding the LSEG and Maple proposals. These were mainly related to patriotism and its repercussions. Patriotism favoured the Maple deal, whilst the repercussions of keeping TMX in Canadian hands supported the London proposal. The parties also disputed which proposal had greater financial merits and risks.

A Patriotism

Patriotic concerns stemmed from the fact that, although the LSEG/TMX merger was described as a merger of equals,²⁵⁸ the proposed structure and results of the transaction gave rise to the impression that Canada was in fact the junior partner in the deal. This was despite the fact that there was an extensive governance package focused on balancing the power between London and Canada.²⁵⁹ The description of the merger as between ‘equals’ was thought necessary to convince regulators and the Government that the merger was not a foreign takeover of Canadian securities exchanges.²⁶⁰ However, the Maple group was concerned that Canada was not equal to London in the merger, and that business and influence would be lost to London.²⁶¹

Maple deployed strong arguments that TMX should, in the interests of patriotism, be kept in the hands of Canadians. It called TMX ‘a great Canadian success story’,²⁶² playing up patriotic sentiments, and claimed that its offer would ‘support high-quality professional jobs

²⁵⁴ Ibid.

²⁵⁵ Ibid.

²⁵⁶ Ibid.

²⁵⁷ Ibid.

²⁵⁸ Shecter, ‘TMX-Maple Deal Demanded Perfection’, above n 23; Erman, ‘TMX Shareholders Should Get Out of This Poker Game’, above n 25.

²⁵⁹ Shecter, ‘TMX-Maple Deal Demanded Perfection’, above n 23.

²⁶⁰ Ibid.

²⁶¹ Erman and Howlett, ‘Shareholders Reject Proposed Merger of TMX and LSE’, above n 249.

²⁶² Tara Perkins and Grant Robertson, ‘Gloves Are Off in TMX Takeover Battle’, *The Globe and Mail* (Toronto), 13 June 2011.

in Canada and [would] ensure TMX Group remains headquartered in Canada'.²⁶³ Maple 'believe[d] an LSE takeover [would] ultimately diminish TMX Group's role in decision making and Canada's standing as a global centre of financial excellence.'²⁶⁴ It argued that the influence of the LSE could cause jobs to leave Canada, and control of Canada's capital markets could shift offshore.²⁶⁵

B Politicians Favour Maple

A number of Canadian politicians also expressed preferences for the Maple proposal's success. Politicians in Ontario and Quebec had indicated their uncomfortableness with a loss of Canadian control.²⁶⁶ They had a lot of influence over TMX because those provinces contained critical regulators.²⁶⁷ The Premier of Quebec, Jean Charest, had publicly indicated his preference that the Maple deal prevailed.²⁶⁸ Mr Charest had indicated that he favoured the Maple offer since it would preserve TMX's Canadian ownership, and would assist in preserving Montreal as a centre for derivatives expertise.²⁶⁹ However, the CEO of the LSE, Xavier Rolet, said that "[t]here [were] undertakings made to keep derivatives in Montreal forever".²⁷⁰ The Finance Minister of Ontario, Dwight Duncan, had called the TSX 'a strategic asset in a strategic industry'.²⁷¹

Nevertheless, politicians opposed to such an important Canadian business being controlled by foreigners would have been reluctant to intervene had the deal proceeded because of the Canadian Government's recent blocking of a BHP Billiton bid to take over Potash Corp of Saskatchewan.²⁷² They were reluctant to give the impression that Canada was unavailable for foreign business.²⁷³ Despite their displeasure, the governments may have allowed the deal to proceed. Ontario's Finance Minister, Dwight Duncan, said that '[w]e would not have been able to, just because we didn't want to allow it to happen, stop it.'²⁷⁴

C Canadian Government Approval Required

²⁶³ Ibid.

²⁶⁴ Ibid.

²⁶⁵ Boyd Erman, 'The Real Damage May Be an Orphaned TMX', *The Globe and Mail* (Toronto), 27 June 2011.

²⁶⁶ Ibid.

²⁶⁷ Ibid.

²⁶⁸ Erman and Howlett, 'Shareholders Reject Proposed Merger of TMX and LSE', above n 249.

²⁶⁹ Erman, 'LSE "Reviewing" Its Bid for TMX Group', above n 224.

²⁷⁰ Ibid.

²⁷¹ Bernard Simon, 'Poll Thumbs Down to TMX-LSE Merger', *Financial Times* (London), 15 February 2011.

²⁷² Erman and Howlett, 'Shareholders Reject Proposed Merger of TMX and LSE', above n 249.

²⁷³ Ibid.

²⁷⁴ Ibid.

Maple's attempts to use patriotism had the potential to influence the general public, regulators, and Canadian TMX shareholders.²⁷⁵ They all could pressure the Canadian Government regarding its decision as to whether to permit the LSE merger proposal under the *Investment Canada Act*,²⁷⁶ despite the fact that it had been assured that approval would be given either unconditionally or on satisfactory terms to both TMX Group and LSEG (considered reasonably).²⁷⁷ The *Investment Canada Act*'s purpose included balancing the potentially competing notions of Canadian national security and the promotion of economic success.²⁷⁸ The Act broadly required that reviewable investments by foreigners could only proceed if approved, and approval required that 'the Minister is satisfied or is deemed to be satisfied that the investment is likely to be of net benefit to Canada'.²⁷⁹ There was therefore significant scope for the relevant minister to consider various factors when deciding whether a 'net benefit' was provided.

D Canada: Closed to Business?

Maple's use of patriotism risked encouraging the perception that Canada was opposed to the merger merely because the LSE was a foreign body.²⁸⁰ The Canadian Government had indicated that it was pro-foreign investment in the Canadian economy,²⁸¹ so Maple's protectionist rhetoric could have discouraged the government from following Maple's position. The Government was particularly concerned about such perceptions of protectionism because of the Potash Corp of Saskatchewan saga within the past year.²⁸²

E Was Maple Motivated by Patriotism?

Maple's spokesman, Luc Bertrand, indicated that the consortium of financial institutions was not acting 'on a patriotic basis'.²⁸³ He said the parties were interested in the financial potential of the enterprise, and that it was 'a business case ... based on solid economics'.²⁸⁴

²⁷⁵ Perkins and Robertson, above n 262.

²⁷⁶ Ibid; *Investment Canada Act*, RSC 1985 (1st Supp), c 28, as current from 12 March 2009 to 28 June 2012 ('*Investment Canada Act*').

²⁷⁷ London Stock Exchange Group Plc and TMX Group Inc, *Press Release*, above n 36.

²⁷⁸ *Investment Canada Act*: 'Recognizing that increased capital and technology benefits Canada, and recognizing the importance of protecting national security, the purposes of this Act are to provide for the review of significant investments in Canada by non-Canadians in a manner that encourages investment, economic growth and employment opportunities in Canada and to provide for the review of investments in Canada by non-Canadians that could be injurious to national security.'

²⁷⁹ Ibid; Frean, above n 134.

²⁸⁰ Perkins and Robertson, above n 262.

²⁸¹ Ibid.

²⁸² Ibid; Perkins, above n 241.

²⁸³ Perkins and Robertson, above n 262.

²⁸⁴ Ibid.

Maple leaders emphasised that their proposal was founded not on patriotic sentiment but on hard business plans.²⁸⁵ However, Leo de Bever, the CEO of Alberta Investment Management Corp (which was a member of Maple), indicated that both patriotism and business interests were influential.²⁸⁶ Notwithstanding the protestations of members of Maple and the concerns of the Canadian Government, in the aftermath of LSEG's failed bid there were accusations in the United Kingdom that Canadian nationalism had won the day.²⁸⁷

F Financial Politics

Maple and the TMX/LSE team also each claimed that their deal would be the best financially. Maple claimed that it had a greater capacity to maintain the dividend than LSEG.²⁸⁸ However, the LSE and TMX Group drew attention to the greater financial flexibility, through lower leverage, that their merged exchange operations would have had.²⁸⁹

LSEG also claimed that there was danger in the large amount of money which Maple would need to borrow for its proposed transaction.²⁹⁰ Maple intended to increase TMX's leverage to over '2.9 times its earnings before interest, taxes, depreciation and amortization'.²⁹¹ This approached the company's debt covenant of 3.5 times, and also a regulatory requirement not to exceed 4 times.²⁹² A senior executive in LSEG, David Lester, said that Maple's proposal would make the resulting entity's profits a quarter of the size of its debts, which could impair its capacity to expand internationally (which Maple had advocated).²⁹³

LSEG also argued that Maple's plan was dangerous because it could concentrate power over Canadian capital markets into the hands of a few pension funds, banks, and brokerages.²⁹⁴

VI CONCLUSION

LSEG's proposed merger was driven by both profit seeking and self-protection. Maple's counterbid, on the other hand, was motivated primarily by profit and nationalism. Its ultimate success created a massive Canadian corporate group with vertical integration which was more efficient.

²⁸⁵ Perkins, above n 241.

²⁸⁶ Ibid.

²⁸⁷ Ibid.

²⁸⁸ Perkins and Robertson, above n 262.

²⁸⁹ Shecter, 'TMX-Maple Deal Demanded Perfection', above n 23.

²⁹⁰ Erman, 'The Real Damage May Be an Orphaned TMX', above n 265.

²⁹¹ Kiladze, 'Maple Group's Next Stop in Bid for TMX Group: Ottawa' above n 224.

²⁹² Ibid.

²⁹³ Costello and Power, above n 120.

²⁹⁴ Erman, 'The Real Damage May Be an Orphaned TMX', above n 265.

Securities regulators raised issues for both transactions, however they did not need to be resolved for LSEG. Maple, on the other hand, made various concessions, including in relation to fees, corporate governance, and conflicts of interest. The Competition Bureau was satisfied with Maple's proposal in light of concessions required by the OSC, despite its potentially significant implications for competition.

The Canadian Government did not need to make the tough decision required under the *Investment Canada Act*, because the LSEG bid did not proceed. However, concerns about protectionism and other political issues were well aired in the public arena.

Maple's road to success was long and hard, spanning over several years. The battle with LSEG involved tactics and ripostes, with each trying to better the other. In the end, TMX Group became the bigger and better TMX Ltd, with Canadian influence over the group firmly entrenched.

Part C NASDAQ – Big Player, Bit Player^{*}

I INTRODUCTION

With domestic and international competition spurring the wave of demutualization of stock exchanges around the globe, shifting regulatory frameworks and the concentration of power from public to private has and will continue to facilitate widespread consolidation of stock exchanges.¹ Those factors responsible for prompting a shift in the organization of stock exchanges from non-profit member-owned organisations to for profit, investor owned, publicly traded stock corporations prove similarly relevant in spurring on the next trend in stock markets – international consolidations.²

NASDAQ OMX (NASDAQ), as a leading international exchange with capabilities that span the globe, typifies the modern international exchange in terms of global reach, growth prospects, competitive threats and the need to remain relevant amidst major rivals such as the New York Stock Exchange (NYSE).

Heralded as the high tech exchange, novel in original form, and ultimately ear marked as a leading United States, and in fact international, exchange rivaling the long-standing NYSE in every way, Nasdaq remains dedicated to a business strategy that continues to emphasize innovation and strive to remain competitive in an increasingly globalised financial services market. In fact, the Nasdaq is the largest US electronic stock market, with approximately 3,200 companies, ‘listing more companies and, on average, trades more days per day than any other U.S market’.³ Nasdaq’s strategy revolves around the widespread dissemination of its market leading *INET* trading platforms, specifically tailored to the needs of exchanges in both developing and developed economies, product diversification and global consolidation, with the 2008 merger with OMX attesting to its strategic growth vision.⁴ Built around four complementary business segments – technology, trade, intelligence and listing – Nasdaq’s product offerings are comprehensive in their scope, and seek to provide clients with unique capital markets infrastructure services, unrivalled in nature and capability.⁵ This chapter will thus seek to expound on Nasdaq’s business strategy through a detailed discussion of its

^{*} The author would like to acknowledge, in particular, the assistance of Luca Del Ciotto with this chapter.

¹ Nu Ri Jung, ‘The Present and Future of the Financial Services Industry: Convergence, Consolidation, Conglomeration, and Collaboration’ (2011) 29 *Quinnipiac Law Review* 729.

² Jake Keaveny, ‘In Defense of Market Self-Regulation: An Analysis of the History of Futures Regulation and the Trend Toward Demutualization’ (2005) 70 *Brooklyn Law Review* 1419, 1438.

³ Nasdaq, *Site Map* <<http://www.nasdaq.com/help/sitemap.stm>>.

⁴ Ibid.

⁵ Nasdaq, *A Powerful Model* <<http://www.nasdaq.com/apowerfulmodel>>.

technological products and offerings, as well as its vision for strategic growth, in the context of global conglomeration and consolidation.

II THE OLD STORY: CONSOLIDATION THROUGH ACQUISITION

A Success and Failure: Nasdaq's Merger attempts

Founded in 1971 by the National Association of Securities Dealers (NASD), Nasdaq was the world's first electronic stock market.⁶ When it began trading on February 8, 1971 as a quotation system, it sought to offer an alternative to the in-person stock transaction system, which the NASD believed burdened investors with inefficient trading and delays.⁷ At inception, however, it was not a trading platform and so did not provide a means to perform electronic trades. The Nasdaq was novel in its function and service, as well as helping lower the spread, being the difference between the bid price and the ask price of the stock).

Whilst being initially unpopular among brokerages as a result of its impact on the spread, Nasdaq eventually assumed the majority of major trades formerly executed by the over-the-counter system of trading, laying the foundation of a major U.S. and indeed global, securities exchange. Over the years, Nasdaq became more of a stock market by adding trade and volume reporting and automated trading systems. Nasdaq was also the first stock market in the United States to start trading online, highlighting Nasdaq-traded companies (usually in technology) and closing with the declaration that Nasdaq was 'the stock market for the next hundred years'.⁸

By 2000, Nasdaq demutualised by converting to publicly owned corporations from privately owned membership organisations in order to gain access to a larger capital base.⁹ In 2006, no more than five years after the NASD spun off the Nasdaq Stock Market, Inc as marking the beginning of its conversion process, the Nasdaq became a national securities exchange, in order to compete with NYSE on all levels.¹⁰ Its decision to seek official exchange status reflected its strategic focus at the time, seeking to compete with the NYSE as the only other registered national securities exchange.

⁶ Ellen Terrell, *History of the American and NASDAQ Stock Exchanges* (October 2012) Library of Congress Business Reference Services < <http://www.loc.gov/r/b/business/amex/amex.html>>.

⁷ Elaine J Ham, 'What is Nasdaq?', *Business News Daily* (online), 9 November <<http://www.businessnewsdaily.com/3403-nasdaq.html>>.

⁸ NASD, *Nasdaq Handbook: The Stock Market for the Next 100 Years: A Complete Reference for Investors, Registered Representatives, Researchers and Analysts* (Probus Professional Pub, Rev Sub ed, 1992).

⁹ Jerry W Markham, *A Financial History of the United States: From Enron-Era Scandals to the Great Recession (2004-2009)* (M E Sharpe, 2011) 149.

¹⁰ Ibid 150.

Since its demutualization and rising status as one of the world's leading and highest trading volume exchanges, it sought to expand its global presence through cross border merger and acquisition activity, seeking to consolidate with its competitors in a bid to remain globally relevant. The following details some attempted (and successful) merger attempts colouring Nasdaq's history, as well as rumoured bids and targets in Nasdaq's now reformed strategy to gain and maintain a global – and lasting – presence as a leading exchange.

1 *The London Stock Exchange*

2006 was characterized by two failed bids for LSE by Nasdaq. Keen to create a trans-Atlantic listings powerhouse, Nasdaq's bids for their English rival were rejected by the majority of the bourse's shareholders.

Nasdaq's first failed bid for LSE saw it build a 14.9% stake in the exchange to gain a foothold in the company in order to take it over. This bid, with a value of about £2.9bn was rejected on 13 March 2006.¹¹

By November 2006, Nasdaq raised its stake in the LSE to 28.75%, proceeding to initiated a hostile takeover on LSE by 20 November 2006, with a deal value of £2.9bn. The bid was rejected unanimously by the LSE's board within hours. Greifeld commented in the wake of the failed hostile bid emphasized that 'Nasdaq will continue to pursue other opportunities to build on its existing position as the world's largest electronic equities exchange, and we look forward to maintaining our strong track record of creating shareholder value through our industry-leading business model and strategy.'¹²

By February 2007, the Nasdaq definitively walked away from the LSE, selling its majority stake in LSE to Borse Dubai as part of an agreement which saw the Middle East operator step aside to allow Nasdaq to take control of Nordic exchange OMX.¹³ Whilst LSE appeared to have been Nasdaq's target for global expansion, it appears unlikely that this will merger will ever be executed. With 2008 marking Nasdaq's acquisition of Stockholm based

¹¹ Phillipa Leighton-Jones and Luke Jeffs, 'The Road to Consolidation – An Exchange Merger Timeline', *Financial News* (online), 15 February 2008 <<http://www.efinancialnews.com/story/2008-02-15/the-road-to-consolidation-an-exchange-merger-timeline-1?ea9c8a2de0ee111045601ab04d673622>>; 'Euronext IPO Successfully Completed – IPO Price: EUR 24 per Share', *Mondo Visione* (online), 5 July 2001 <<http://www.mondovisione.com/news/euronext-ipo-successfully-completed-ipo-price-eur-24-per-share/>>.

¹² 'Nasdaq Fails in Takeover Bid for London Stock Exchange - Business - International Herald Tribune', *New York Times* (online), 11 February 2007 <<http://www.nytimes.com/2007/02/11/business/worldbusiness/11iht-nasdaq.4549290.html>>

¹³ Jonathan Sibun, 'Nasdaq Sells LSE Stake to Borse Dubai', *The Telegraph* (online), 20 September 2007 <<http://www.telegraph.co.uk/finance/markets/2816122/Nasdaq-sells-LSE-stake-to-Borse-Dubai.html>>.

exchange OMX, it seems to have implemented an alternate strategy aimed at securing a competitive place in European capital markets.

2 The Singapore Stock Exchange

With the LSE rejecting the Nasdaq bid made on 10 March 2006, news of Nasdaq's rumoured interest in a take over of the SGX spread through Wall Street and the world's financial centres.¹⁴ SGX, however, publicly denied it was ever in any merger talks with the Nasdaq exchange, some two days after media reports of the rumoured takeover on 6 April 2006.¹⁵

3 The NASDAQ OMX Merger

In February 2008, Nasdaq acquired Nordic powerhouse stock exchange OMX via combination. To complete the deal, and appease the multijurisdictional regulations and requirements, Nasdaq was required to make an agreement with UAE exchange Borse Dubai to sell 19.99% of Nasdaq to them in exchange for the shares it then held in OMX.

The agreement struck between the two exchanges resulted in Nasdaq having sold 28% out of the 33% stake it then held in the LSE to Borse Dubai. Borse Dubai's purchase of the Nasdaq's stake in LSE proved symptomatic of the global push towards exchange consolidation that characterized the time. Borse Dubai's interest in the LSE was spurred by the Middle East's mandate to diversify away from reliance on oil and gas, competing with the gulf cities – particularly Qatar in the context of LSE – to become the Middle East's pre-eminent financial centre.¹⁶ Where 2007 was marked by the UAE's bid to diversify its assets amidst a booming economy, and boost its credentials as a financial hub in the Middle East by forging ties with a well known international entity such as LSE, this year saw Borse Dubai sell its remaining 17.4% stake in the entity.¹⁷ Even though Dubai's economy is booming again, the sale is likely no surprise given the not so distant memory of a crash in the wake of the GFC – which left the emirate heavily in debt with several of its high profile investments worth less than the purchase price. Accordingly, the LSE sale reflects the emirate's apparent

¹⁴ Uma Shankari, 'Talk of Nasdaq Takeover Propels SGX', *Business Times Singapore* (online), 7 April 2006 <<https://global.factiva.com/>>.

¹⁵ Goh Eng Yeow, 'SGX Slides Following Denial of Nasdaq Takeover Talks', *Straits Times* (online), 8 April 2006 <<https://global.factiva.com/>>.

¹⁶ Simon Bowers, 'Gulf Rivals Nearly Snap up Half of the London Stock Exchange', *The Guardian* (online), 21 September 2007 <<http://www.theguardian.com/business/2007/sep/21/9>>.

¹⁷ Ibid.

focus on cleaning up its finances at home as it restructures many of its key holding companies, also selling some assets to free up cash and redeploy it.¹⁸

Also as part of the transaction, Nasdaq became a 33 1/3% shareholder in DIFX, Dubai's international financial exchange.¹⁹ By 2009, Nasdaq OMX Nordic, part of the Nasdaq OMX Group, sought to further its influence over the European region, finally completing its process to also integrate all Baltic exchanges into the Group.

The transaction proves consistent with Nasdaq's global strategy, helping it achieve its goal of becoming a 'new type of exchange company... unique in its ability to serve customers at multiple levels, from trading platforms supporting multiple asset classes to listings, financial services technology, and data and financial products',²⁰ said Bob Greifeld, Chief Executive Officer of Nasdaq. The transaction served to facilitate the exchange's strategic objectives of becoming 'a diversified global exchange operator'.²¹ The acquisition kick-started strategic developments for Nasdaq, resulting in the opening of the 'NASDAQ OMX Europe' multilateral trading facility in London, representing "the transformation of Nasdaq from a U.S-focused cash equity exchange",²² creating a new source of pan-European competition, breaking down the pricing monopolies that once characterized the European market for stock exchanges.

As per the Definitive Proxy Statement filed with the SEC pursuant to Section 14(a) of the Securities Exchange Act, Nasdaq enumerated several strategic benefits behind the acquisition. These included:²³

- (i) Have strategic and technological benefits, such as:
 - a. Creating a premier global exchange company with an average daily trading volume of 7.4 million trades, representing a value of approximately \$61 billion, and with approximately 4,000 listed companies from 39 countries with an aggregate market capitalization of approximately \$5.5 trillion;
 - b. Creating the world's largest companies listed on their respective marketplaces;
 - c. Having a leading market share of listings in such industries as technology, software, *etc.*

¹⁸ Nikhil Lohade, 'Borse Dubai to Sell Its Stake in London Stock Exchange Group', *The Wall Street Journal* (online), 25 March 2015 <<http://www.wsj.com/articles/borse-dubai-to-sell-its-stake-in-london-stock-exchange-group-1427307108>>.

¹⁹ Nasdaq, 'NASDAQ Completes OMX Transaction to Become the NASDAQ OMX Group, Inc.' (Press Release, 27 February 2008) <<http://ir.nasdaqomx.com/releasedetail.cfm?ReleaseID=296336>>.

²⁰ Ibid.

²¹ Ibid.

²² Ibid.

²³ NASDAQ OMX Group Inc, *Form 14A - Proxy Statement (Definitive)* (19 November 2007) 45, <<http://www.sec.gov/cgi-bin/browse-edgar?action=getcompany&CIK=0001120193&type=DEFM14A&dateb=&owner=exclude&count=40>>.

- d. Creating a world leader in the provision of exchange technology, with
 - i. OMX having been a pioneer in creating a truly integrated cross-border stock market and also has created a world-renowned technology customer base of equity, debt and derivatives exchanges with its systems being used by over 60 marketplaces in more than 50 countries worldwide, including Hong Kong, Singapore, Australia and the U.S.; and
 - ii. Nasdaq laying claim as the world's first electronic stock exchange, pioneering electronic trading and continuing to innovate over the past thirty years to now become the fastest, most efficient platform in the U.S
- e. Providing increased access to global equity capital through greater liquidity pools, advanced speed of execution and integrated cross-border trading capabilities;
- f. Combining the capabilities of OMX, which is an integrated cross-border stock market with a customer base of equity, debt and derivatives, with the Nasdaq's fastest U.S. trading platforms;
- g. Benefiting from new technologies and combined electronic trading platforms;
- h. Using its combined data vendors to enhance market transparency;
- i. Combining technology businesses and assuring new growth opportunities;
- j. Helping investors benefit from higher trading volumes, a common IT interface and positive portfolio diversification.
- (ii) Enhance product diversification and expand the Company's networks, including:
 - Being highly competitive in derivatives market, given the Nordic Exchange was considered at the time of the acquisition as Europe's third largest marketplace for trading and clearing derivatives. The combined company would thus capture the high growth potential in global derivatives;
 - Developing innovative data products and combined indices for stocks and derivatives, and increasing geographic and sector diversification;
 - Extending the OMX's Nordic distribution network through an international network with cooperating exchanges.
 - Providing better data business with improved global distribution and value-added services to market participants.
- (iii) Realise the high synergy potential by 2010, namely, \$150 million of annual pre-tax synergies, including \$100 million cost synergies from rationalization of the IT-systems and data centers, reduced capital and procurement expenditures; and \$50 million of revenue synergies from deeper liquidity pools, increased cross-border trading and international listings.]
- (iv) Have better managerial cooperation. The OMX Transaction Agreement (PS, at 87) indicates that Directors and managers of the combined entity will consist of 16 directors, including 9 from Nasdaq, four from OMX and two from Borse Dubai. Three directors from OMX and both from Borse must be independent.

On point (iii), Guseva commented that 'there is no comprehensive quantitative study providing monetary evaluation of the "synergies" and whether they have been partially achieved since the merger'.²⁴

The statement similarly discussed risks relating to Nasdaq's, OMX's and the combined company's business, as factors driving the need to consolidate on a global scale. Competition

²⁴ Yuliya Guseva, 'Cross-Border Mergers Of Securities Exchanges, Regulation Of Foreign Brokers And Dealers, And Related Reforms', (Outline and Annotated Bibliography, Columbia Law School/Business School Program in the Law and Economics of Capital Markets, 24 June 2010) 5 <<https://web.law.columbia.edu/sites/default/files/microsites/capital-markets/cross-border-mergers.pdf>>.

is emphasized as the main driver behind the need for global expansion.²⁵

The risks discussed at the time of the merger emphasized the threat of increased competition in the securities market industry, including competition for trading services, listings and financial products from other exchanges and market centres. This competition included both product and price competition and could increase as a result of the registration of new exchanges and market centers in the United States and Europe.

In addition, the liberalization and globalization of world markets had resulted in greater mobility of capital, greater international participation in local markets and more competition. Both in the U.S. and in other countries, the competition among exchanges and other execution venues has become more intense.²⁶

Whilst topical at the time of the merger, the fact still remains that the structure of the securities industry has changed significantly through demutualisations and consolidations. In response to growing competition, many marketplaces in both Europe and the United States have demutualized to provide greater flexibility for future growth. The securities industry was also experiencing consolidation, creating a more intense competitive environment.²⁷ In addition, a high proportion of business in the securities market had been becoming (and continues to become) increasingly concentrated in a smaller number of institutions and the combined company's revenue may therefore become concentrated in a smaller number of customers.²⁸ Examples of these new competitive forces, as at the time of the merger, included:

- Since 2006, eight investment banks have announced that they intend to set up a multilateral trading facility in Europe, also known as Project Turquoise (note that despite Nasdaq's inet trading technology being pegged as the consortiums preferred platform, it ultimately selected Sweden's Cinnober as its trading platform).²⁹
- Since 2006, 14 investment banks have announced that they intend to set up a multilateral trade reporting facility in Europe, known as Project Boat
- Alternative trading platforms such as Equiduct, Chi-X and Plus Markets

²⁵ NASDAQ OMX Group Inc, *Form 14A*, above n 23.

²⁶ Reena Aggarwal and Sandeep Dahiya, 'Demutualization and Public Offerings of Financial Exchanges' (2006) 18 *Journal of Applied Corporate Finance* 96, 105.

²⁷ *Ibid.*

²⁸ NASDAQ OMX, 'Group Annual Report (10-K)' (Company Report, 2009).

²⁹ Henry Teitelbaum, 'Markets: Green Still Means Go', *Institutional Investor* (online), 17 Jan 2008 <<http://www.institutionalinvestor.com/article.aspx?articleID=1854533#.VVPnylwxFyg>>.

- Alternative trade reporting platforms such as Reuters Trade Publication;
- The proposed combination of Deutsche Börse AG and International Securities Exchange Holdings, Inc.; {did this happen}?
- Electronic trading systems specializing in large volume trades, such as LiquidNet, Pipeline Trading and Investment Technology Group's POSIT platform;
- The creation of NYSE Euronext, Inc. in April 2007
- The Chicago Stock Exchange, Inc., the Philadelphia Stock Exchange, Inc, the National Stock Exchange, the International Securities Exchange LLC, and the Chicago Board Options Exchange all have investment agreements with other participants in the securities industry
 - Note that later in 2008, Nasdaq acquired Boston Stock Exchange, and Philadelphia Stock Exchange, in line with its strategy to enter into the business of trading equity derivatives.³⁰
- New ECNs operating in the U.S. cash equities trading market, such as Direct Edge, Lava Flow and BATS; and
- The International Securities Exchange's and the Chicago Board Options Exchange's launch of cash equities exchanges in September 2006 and March 2007, respectively.

In 2008, the intensely competitive nature of Nasdaq's industry called for a bid to strengthen its global presence and forge secure transatlantic network. In 2008, NYSE Euronext was considered the Nasdaq's most significant competitor, serving as a major prompt behind the Nasdaq's bid to merge with a strong European exchange. Still true now, NYSE Euronext, among other U.S. exchanges such as BATS Global Markets and Direct Edge, and the global powerhouses such as Deutsche Borse, the Tokyo Stock Exchange and LSE continue to pose significant competitive threats to all areas of Nasdaq's business, offering a range of services comparable to those offered by Nasdaq.³¹

Since the Nasdaq merger with OMX, different forms of competition have spurred a different strategic emphasis for the Nasdaq. The traditional model, where each exchange or exchange-related business developed its own technology internally has and continues to evolve as many operators realize the significant cost savings that come with buying technology that has

³⁰ Nandini Sukumar and Matthew Leising, 'Nasdaq to Buy Boston Stock Exchange for \$61 Million', *Bloomberg* (online), 2 Oct 2007 <<http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aPC uumZdpR0>>.

³¹ NASDAQ OMX, above n 28.

already been developed, and can be tailored to the unique needs of a particular exchange.³² NYSE Euronext, LSE, among others, now compete with Nasdaq as a technology provider to the exchange industry, and will continue to rival the Nasdaq in becoming the primary developer of leading market technology.

4 The Boston Stock Exchange and Philadelphia Stock Exchange

By August 2008, Nasdaq had completed its acquisition of both the Philadelphia Stock Exchange and the Boston Stock Exchange. Its purchase of the Philadelphia Stock Exchange sought to expand its global presence in derivatives markets. Prior to its acquisition, the Philadelphia Stock Exchange was the nation's oldest stock exchange; and its purchase resulted in the Nasdaq operating the third largest options market in the U.S.

Its purchase of the Boston Stock Exchange resulted in Nasdaq gaining another venue for trading, allowing brokerages to execute transactions more easily by posting quotes on both markets. The acquisition will also give Nasdaq control of the regulatory arm of Boston Options Exchange as it prepares to enter the faster-growing business of trading equity derivatives. It should be noted that the acquisition did not include the Boston Options Exchange, which later sold a majority stake to Montreal Exchange Inc., owner of Canada's derivatives market.³³ In fact, by 2009, The Montreal Exchange had over a 51% equity holding in the Boston Options Exchange.³⁴

5 NYSE Euronext

2011 saw a failed bid for NYSE Euronext by Nasdaq, who sought to acquire NYSE Euronext in order to derail a planned merger between NYSE Euronext and the Deutsche Borse. With the Justice Department planning to block the proposed transaction for antitrust issues, the bid was ultimately withdrawn by NASDAQ OMX (together with commodities futures and derivatives marketplace IntercontinentalExchange).

On the merger, Nasdaq CEO Robert Greifeld commented 'we saw a unique opportunity to create more value for stockholders and strengthen the U.S. as a center for capital formation amid an ongoing shift of these vital activities and jobs outside of our country,' in line with its

³² Ibid.

³³ Nandini Sukumar, 'Nasdaq Says No Merger Discussions with LSE, Euronext', *Bloomberg Business*, 26 February 2014 <<http://www.bloomberg.com/news/articles/2014-02-26/nasdaq-says-no-merger-discussions-with-lse-euronext>>.

³⁴ Ibid.

strategy for global consolidation to remain relevant.³⁵ As reported by DealBook New York Times, ‘the withdrawn bid is another failed attempt by Mr. Greifeld and Nasdaq to find a partner as a wave of consolidation washes over the world’s exchanges. In 2006, it began a long but ultimately frustrated bid to acquire the London Stock Exchange.’³⁶

III NEW DIRECTIONS: GROWTH THROUGH PRODUCT DIVERSIFICATION

Nasdaq appears more focused on the US in recent years, seeking to expand through product diversification within its US offerings.³⁷ 2013 saw the acquisition of electronic Treasuries-trading platform eSpeed from Amercian global financial services company BGC Partners Inc, so providing the exchange operator ‘an entry into one of the world’s largest and most liquid cash markets’.³⁸ This deal was heralded as giving Nasdaq more exposure to fixed income markets, ‘fitting into the strategy of expanding in asset classes beyond stock trading’.³⁹ The eSpeed deal differentiates Nasdaq in fixed income from other exchange operators, which have mainly been focused on interest rate swap clearing and swap-like futures trading. The acquisition marks Nasdaq customer focused strategy that seeks to provide an electronic platform which customers can use to access a variety of tradable financial products.⁴⁰

Nasdaq also acquired Thomson Reuters Corp’s investor relations, public relations and multimedia services unit in 2012/2013, seeking to diversify its operations into businesses that do not depend on trading. The acquisition marks a clear strategy which seeks to sell additional services to companies that list on its exchanges, seeking to ‘draw more revenue from its corporate customers’, via helping companies communicate with investors and media and create and distribute video presentations.⁴¹

Beyond domestic borders, Nasdaq’s bid to remain globally competitive saw its launch of ‘NLX’ in 2013, a Europe-based fixed-income futures trading platform to compete with Deutsche Boerse AG-owned Eurex and Intercontinental Exchanges’ London-based LIIFE - following the 2013 multi-billion dollar purchase of NYSE Euronext by Intercontinental

³⁵ Azam Ahmed, ‘Nasdaq Drops Bid to Buy NYSE Euronext’, *The New York Times* (online), 16 May 2011 <http://dealbook.nytimes.com/2011/05/16/nasdaq-drops-its-bid-to-buy-nyse-euronext/?_r=0>.

³⁶ Ibid.

³⁷ Sukumar, above n 33.

³⁸ John McCrank, ‘Nasdaq to Buy eSpeed Platform for \$750 Million’, *Reuters*, 1 April 2013 <<http://www.reuters.com/article/2013/04/02/net-us-nasdaq-acquisition-idUSBRE9300J720130402>>.

³⁹ Ibid.

⁴⁰ Ibid.

⁴¹ John McCrank, ‘Nasdaq to Buy Thomson Reuters PR, IR Units for \$390 Million’, *Reuters* (online), 12 Dec 2012 <<http://www.reuters.com/article/2012/12/12/us-nasdaq-thomsonreuters-idUSBRE8BB0SP20121212>>.

Exchange (ICE).⁴² NLX's first years of trading have proved profitable for Nasdaq, gaining significant traction in the market for European derivatives contracts. In fact, 'NLX has now traded over 14 million lots and has a 30-day moving-average market share of 16 percent in Euribor, the world's second-largest short-term interest rate contract after Eurodollar'.⁴³

While NLX has shown positive signs and has definitely exited the start-up phase, its impact on competitors such as LIIFE and Eurex is still unknown, even in spite of securing some market share.

NLX demonstrates Nasdaq's strategic vision to remain at the forefront of product offerings. In fact, NLX is rumoured to be considering (along with most European competitors such as Eurex and LSE) swap futures⁴⁴, being standardized contracts that mimic the economic exposure of traditional over-the-counter (OTC) interest rate swaps but are traded on an exchange and require less margin. According to Nadja Ubran, SVP, product development, Eurex, "The swap market is a big market with many opportunities due to the fact that the regulatory environment will lead to structural changes, so of course every platform or exchange is taking the opportunity to take a part of this business."⁴⁵ Though rumoured, NLX has yet to definitely state whether these plans will come to fruition.

In line with product diversification, Nasdaq has also launched "Nasdaq Private Market", a pre-IPO marketplace for trading in shares of unlisted companies via a joint venture with small trading platform SharesPost Inc, tapping into increasing investor interest in private firms. The new venture sought to help the exchange rebuild its reputation as the exchange of choice for unlisted companies, after it was criticized for its role in the botched Facebook Inc IPO in May 2012.⁴⁶ Just as the JOBS Act kick-starts bigger markets for shares of privately held companies, NASDAQ Private Market sought to capitalize on the growth-company market,

⁴² 'ICE Buys NYSE-Euronext: The End of the Street', *The Economist* (online), 16 Nov 2013 <<http://www.economist.com/news/finance-and-economics/21589913-improbable-takeover-highlights-uncertain-future-share-trading-end>>.

⁴³ Clare Hutchison, 'Nasdaq NLX No Longer a Startup, Ready to Take on Incumbents', *Reuters London* (online), 2 June 2014 <<http://uk.reuters.com/article/2014/06/02/uk-nasdaq-derivatives-idUKKBN0ED01C20140602>>.

⁴⁴ Note that GMEX has already launched a form of swap futures; GMEX has developed its own form of swap future by basing the contract on an underlying index designed to reflect pricing in the interest rate swap market in real time. The constant maturity future is linked to GMEX's proprietary Interest Rate Swap Index Average and tracks every point on the yield curve, retaining its maturity throughout the lifetime of the trade. But not really a futures swap; what differentiates GMEX's launch is that this contract is not an attempt to futurise a swap but to launch futures on an index which replicates the daily interest-rate swap market.

⁴⁵ Jon Watkins, 'Innovation Spotlight: Swap Futures', *The Trade News* (online), 17 Nov 2014, <http://www.thetradenews.com/news/Trading__Execution/Industry_issues/Innovation_spotlight__Swap_futures.aspx>.

⁴⁶ Aman Shah, 'Nasdaq, SharesPost to Set Up Market for Unlisted Stocks', *Reuters US* (online), 6 Mar 2013 <<http://www.reuters.com/article/2013/03/06/us-nasdaq-sharespost-idUSBRE9250KT20130306>>.

affording businesses access to institutional investors for capital and employee liquidity, allowing them the flexibility to decide when and if going public is appropriate. Nasdaq are part of a growing number of players like SecondMarket, AngelList, Funders Club, WeFunder and Equidate that allow private companies to raise capital from a broader number of investors beyond traditional VC firms. The platform is used to let early employees sell their shares while managing who can buy and sell shares, how many shares can be sold at any time, and the timing of transactions and the depth of financial disclosures to prospective investors.⁴⁷ This ultimately allows such companies to take control of the secondary market for their shares.

Nasdaq Private Market has and will continue to deliver strategic benefits for the exchange, allowing them to foster relationships early with growth-stage companies so luring them into their exchange once they go public (if ever). More, it will assist companies start a dialogue with long term institutional investors, who may end up holding stock for years on public markets.⁴⁸

2015 has already seen the launch of Nasdaq Futures Exchange (NFX), seeking to compete against the U.S.'s two largest-energy exchange operators, ICE and CME Group Inc. Firms that trade on NFX will clear through the Options Clearing Corp, rather than Nasdaq's own clearing firm (as ICE and CME do as a means of increasing profits per trade). The venture aims to grab 10% of energy futures for Nasdaq within two years, which would add some \$50 million a year to the company's bottom line. The new market, which will include futures and options contracts for U.S. natural gas, Brent crude oil, U.S. power and other products, is expected to be ready for trading by the end of the summer.⁴⁹ Nasdaq Futures would use an existing futures exchange Nasdaq acquired when it bought the Philadelphia Stock Exchange in 2007 (now named 'NASDAQ OMX PHLX') for about \$650 million, as well as being connected to Trading Technology's new platform 'TT', so expanding Nasdaq's commodities business with futures and options on the aforementioned key energy benchmarks, including oil and natural gas and U.S. power.⁵⁰

⁴⁷ Kim-Mai Cutler, 'Nasdaq Finally Launches Its Market for Privately-Held Companies', *The TechCrunch* (online), 5 March 2014 <<http://techcrunch.com/2014/03/05/nasdaq-finally-launches-its-market-for-privately-held-companies>>.

⁴⁸ Ibid.

⁴⁹ Bradley Hope and Nicole Freidman, 'Nasdaq to Launch Energy Futures Market', *The Wall Street Journal* (online), 11 March 2015 <<http://www.wsj.com/articles/nasdaq-to-launch-energy-futures-market-1426082521>>.

⁵⁰ 'Trading Technologies Announces New Platform; Will Connect to Nasdaq Energy Futures' (Press Release, 11 March 2015) <<http://www.futuresmag.com/2015/03/11/trading-technologies-announces-new-platform-will-connect-nasdaq-energy-futures>>; Trading Technologies, 'OTC Global Holdings' EOXLive Active Markets to be Available on Trading Technologies' New TT Platform' (News Releases, 11 March 2015) <

The launch of Nasdaq Futures may also allow Nasdaq to offer a more diverse suite of products to existing clients who already use Nasdaq to trade stock based products, able to use the same accounts to execute multiple trades across different asset classes and types.

Nasdaq's diversification strategy has also seen it add to its indexing business, with the acquisition of Mergent Inc, in 2012 and American index and analytics provider Dorsey Wright and Associates earlier this year.

The acquisition of Mergent Inc⁵¹, including Indxis, has made Nasdaq one of the world's largest dividend-focused index providers in the market.

This acquisition of Dorsey Wright similarly seeks to achieve Greifeld's mandate for growth. Prompted by LSE Group's billion dollar acquisition of Russell Investments, the Dorsey Wright acquisition will seek to expand Nasdaq's current command of the Exchange Traded Fund (ETF) market, gaining control of over 17 of Dorsey Wright's ETFs and 69 of its smart-beta ETFs. The acquisition attests to Nasdaq's strategic interest in smart-beta indexing, expected to generate returns in the long run.⁵² In addition to the ETFs, Nasdaq's Global Indexes division will also gain access to over \$45 million in invested assets to Dorsey Wright's smart-beta indexes and about \$105 billion benchmarked to existing Nasdaq indexes. Dorsey Wright licenses its indexes to investment management firms PowerShares and First Trust. These license agreements should help Nasdaq generate higher index licensing revenues with a potential to grow its subscriber base to other investment adviser firms. According to management, the acquisition fits in strategically with the company's vision of future in the indexing market space.⁵³

IV CONTINUED EMPHASIS: TECHNOLOGY

As discussed, the Nasdaq recognizes the need to become a market leader in exchange technology. With the European landscape '...continuing to adapt to the competitive forces

<https://www.tradingtechnologies.com/news/150311-otc-2/>>; Trading Technologies, 'Trading Technologies to Connect to Nasdaq Energy Futures' (News Releases, 11 March 2015) < <https://www.tradingtechnologies.com/news/150311-nasdaq-2/>>.

⁵¹ Mergent is the firm behind the Dividend Achievers Indexes, the same roster of dividend-focused benchmarks underlying ETFs such as the \$14 billion Vanguard Dividend Appreciation ETF (NYSEArca:VIG), as well as a number of Invesco PowerShares funds including the \$285 million PowerShares Dividend Achievers Portfolio (NYSEArca:PFM) and the \$722.7 million PowerShares International Dividend Achievers Portfolio (NYSEArca:PID).

⁵² Smart-beta indexing is different from traditional market cap-based indexes as they weigh in certain other factors to gauge value. Dorsey Wright predominantly operates in relative strength indexes, which take into account market performance.

⁵³ Trefis Team, 'NASDAQ OMX Adds to Indexing Business With \$225 Million Acquisition', *Forbes* (online), 1 July 2015 <<http://www.forbes.com/sites/greatspeculations/2015/01/07/nasdaq-omx-adds-to-indexing-business-with-225-million-acquisition/>>.

released by MiFID in November 2007' new Multilateral Trading Facilities (MTFs) such as Chi-X, Turquoise, and BATS, among others) continue to gain a significant share of electronically matched volume, and have made the Nasdaq's emphasis on maintaining its historical status as an innovative tech exchange all the more necessary. These regulatory developments in Europe have paved the way for many of the Nasdaq's global competitors to engage in '...aggressive price competition by reducing the trade execution transaction fees that charge their customers'.

Accordingly, Nasdaq continues to 'provide a comprehensive suite of trading solutions'.⁵⁴ Nasdaq still serves as the pioneer of electronic trading, and its core business strategy remains dedicated to technological improvements aimed at continually revolutionizing the way markets operate. Since its inception over four decades ago, Nasdaq's commitment to extensive R&D has 'produced low-latency, functionally rich trading systems that can help venues reliably scale and adapt to changing market conditions'. Whilst its historical strong hold over market technology is not as historically strong, Nasdaq technology still powers 1 in 10 securities transactions around the world, with its *INET* matching engines having been 'installed in 55 markets in 47 organisations in 45 countries across 6 continents'.⁵⁵

Overall, Nasdaq has thus developed technological products that range from trading (matching and execution), surveillance, trade-risk management, post trade clearing and corporate governance.

A Trading Technology – Matching and Execution

Nasdaq's matching and execution solutions aim to provide functionally-rich platforms that support trading in any asset, able to adapt as businesses expand into new asset classes or seek to offer additional services. The Nasdaq *INET* platform provides matching, execution and clearing solutions, and is available in two forms, *Genium INET* and *X-Stream INET*.

The *Genium INET* is Nasdaq's own in-house trading platform, which is more focused on speed and high volumes. This is marketed to exchanges operating in developed markets, given its more varied asset class offerings, and more involved implementation process.⁵⁶ Its multi-asset, multi-market capabilities make *Genium INET* suitable for exchanges that need customization beyond the boilerplate matching and execution services, and have more

⁵⁴ Nasdaq, *X-Stream Trading* <http://www.nasdaqomx.com/digitalAssets/97/97288_x-stream-trading.pdf>

⁵⁵ Ibid.

⁵⁶ Ibid.

sophisticated requirements.⁵⁷

The *X-Stream INET* platform is used by more than 30 exchanges across the globe, divided into two versions. The first is an ‘out of the box version’, which covers equities and fixed income. The more customized version includes derivatives. Both versions share the same basic technical specifications. X-stream is marketed to exchanges that are looking to keep their cost low, able to be adapted by customers who may require more advanced features.⁵⁸

Despite the other options available, (and offered by groups such as the London Stock Exchange and NYSE Euronext), *X-Stream INET* serves as the most widely deployed matching engine in the world, ‘combining extraordinary performance with extensive functionality to meet current and future business and performance requirements. X-stream provides the operational efficiencies needed to keep technology costs in line, with the comprehensive functionality necessary to fully meet client demands, no matter how unique’.⁵⁹

B Post Trade Products – Clearing

Where the prevailing regulatory environment pre the Global Financial Crisis failed to adequately protect against systemic and operational risk, the regulatory mandate in several jurisdictions has focused upon the role of clearers. Specifically, the regulatory mandate of central clearing seeks to standardize certain swaps, ultimately promoting transparency and allowing market participants to mitigate their counterparty credit risk to dealers.⁶⁰ In the US, Dodd-Frank reform has sought to enhance the role of Central Clearinghouses (CCPs) in certain derivative contracts. Pre Dodd-Frank, most swaps were traded on a bilateral, principal to principal basis with your ultimate counterparty being the entity with whom you executed the trade. Under the new mandatory regime, transactions must be submitted through a clearing member, acting in an agency capacity, to a Central Clearinghouse (CCP) for clearing. Once cleared, the Clearinghouse is the counterparty to all trades, and the US regulatory bodies (CFTC and SEC) require that the Clearinghouse has appropriate tools and procedures for risk mitigation. The new regime directs regulatory power to the SEC for

⁵⁷ Nasdaq, *Matching and Execution Solutions* (2015) <<http://business.nasdaq.com/tech/trading/matching-and-execution/index.html>>.

⁵⁸ Nasdaq, *X-Stream Trading Factsheet* (2015) <http://business.nasdaq.com/Docs//x-stream-trading_tcm5044-11862.pdf>.

⁵⁹ Ibid.

⁶⁰ Goldman Sachs, ‘Financial Reform: Dodd-Frank Central Clearing’ (Fact Sheet, Goldman Sachs Asset Management, 2012) <<http://www.goldmansachs.com/gsam/worldwide/insights/FinReg/clearing-fact-sheet-2.pdf>>.

security based swaps, and to the CFTC for all other swaps, such as swaps on all rates and commodity products, broad based indices, FX options and non-deliverable FX forward contracts. Similar reform under the European Market Infrastructure Regulation (EMIR) and Basel III has mandated the role of CCP in derivative contracts, carrying associated implications for clearing houses across the globe.

Such regulatory reforms will result in increased operational complexity, where ‘the introduction of central clearing, coupled with the substantial remaining volume of bilateral trading, will require that two market processes be put in place by virtually all market participants’.⁶¹ More, the combined impact of the legislation being the imposition of mandatory initial margin payments for both cleared and non-cleared transactions, there will be a substantial increase in the value of collateral held against all OTC derivatives by approx. \$2 trillion, an increase of 50% from current levels.⁶² Such an increase will make collateral optimisation a strategic priority for exchanges, where those who can efficiently manage margin across cleared and non-cleared derivatives enjoying a significant competitive advantage.

The new regulatory context thus demands ‘improved transparency and risk management capabilities, tighter capital requirements and ability to connect to and transact business with a much larger number of venues’, and carry high update costs in dealing with this enhanced operational complexity.⁶³

The post trade clearing technology developed by Nasdaq serves to meet the new regulatory brief. Already in use by 13 clearinghouses globally and backed by 20 years of knowledge and clearing experience, Nasdaq’s post trade solutions promise ‘robust functionality needed to meet today’s challenges, and the adaptability and innovation to help future-proof organisation[s] for whatever comes next’.⁶⁴

The *Genium* INET Clearing technology forms part of the *Genium* specific platform, used for exchanges and clearing houses in need of high-velocity clearing capabilities, settlement and collateral and risk management. *Genium* is ideally suited for high volume marketplaces that

⁶¹ JP Morgan, ‘Regulatory Reform and Collateral Management: The Impact on Major Participants in the OTC Derivatives Markets’ (Publication, 2012) <https://www.jpmorgan.com/tss/DocumentForEmail/Regulatory_Reform_and_Collateral_Management/1320476294035>.

⁶² Executive Office of the ISDA, *Derivativeness* (6 September 2011) <<http://isda.derivativeness.org>>.

⁶³ Nasdaq, *Post-Trade Clearing: Genium INET & X-Stream INet* (2015) <<http://business.nasdaq.com/tech/post-trade/clearing/index.html>>.

⁶⁴ Ibid.

require a central counterparty (CCP) solution to clear and settle trades across asset classes, markets and currencies and can benefit from real-time position handling to manage risk exposure. Seeking to capture all market needs in a bid to out do its cheaply priced competitors, Nasdaq also offers the post trade risk management platform Sentinel, which if combined with *Genium* clearing technology will allow clearinghouses to manage a its risk across a wide variety of asset categories, including OTC produces and corporate actions.⁶⁵

The *X-Stream* INET clearing technology similarly provides clearing, settlement and risk management. Whilst ideally suited for clearing of OTC derivatives, *X-Stream* has the capacity of handle a broad range of assets to manage a wide variety of business needs. *X-stream* provides the full value chain – matching/tracing, clearing and Central Securities Depository's (CSD) – within the same technology, from orders settled to registry bookings.

C Surveillance, Trade Risk Management and Governance, Risk and Compliance

In addition to trading platforms, Nasdaq provides surveillance, trade risk management and risk and compliance services and software to exchanges across the world. Nasdaq's SMARTS surveillance technology powers over 100 market participants globally.⁶⁶

In terms of risk and compliance software, Nasdaq's B Wise eGRC platform provides as the cornerstone of the Nasdaq's enterprise Governance, Risk and Compliance (eGRC) offering, allowing companies to identify, understand, measure and manage key financial and organizational risks on a holistic level. The B Wise eGRC Platform allows organizations to track, measure and manage key risk indicators for multiple parts of the business all in one integrated system. Beyond B Wise, Nasdaq similarly offers Directors Desk – a platform aimed at streamlining the sharing of mission-critical information via the web or tablet – as well as incident reporting in the form of a Whistleblower Hotline.

Nasdaq's technological offerings are varied in their form, used by exchanges globally. Nonetheless, many of Nasdaq's competitors have and will continue to engage in aggressive price competition by reducing the trade execution fees charged to customers, offering similar suites of products and services. In response, Nasdaq has year on year reduced the trade execution fees it charges to customers in a bid to maintain its market leading position in the provision of exchange technology. Even in spite of price challenges, Nasdaq's innovative

⁶⁵ Ibid.

⁶⁶ Nasdaq, *Surveillance: Cross-Market, Cross-Asset Surveillance Technology* (2015) <<http://business.nasdaq.com/tech/surveillance/index.html>>.

history has meant that the widespread licensing of its technologies has not diminished, placing the Nasdaq in a strong position as a global player in potentially making marketplaces powered by Nasdaq technology rife for acquisition given the ease of compatibility between Nasdaq itself, and any exchange that relies on its technology.⁶⁷

⁶⁷ NASDAQ OMX, above n 28.

Part D Singapore and Sydney – Politics, Politics, Politics*

I THE BID

The ASX Limited (ASX) and Singapore Exchange Limited (SGX) announced, on October 25, 2010, that they had entered into a merger implementation agreement (MIA). The proposed merger was a scheme of arrangement, which is a mechanism available under s 411 of the *Corporations Act 2001* (Cth) (*The Corporations Act*),¹ used by SGX to acquire all issued ordinary shares in ASX.² The scheme was valued at AUD \$8.4 billion.³ Each ASX shareholder would be paid a combination of AUD \$22 in cash and 3.473 newly issued SGX ordinary shares, which in total was equivalent to about AUD \$ 48 in value per ASX ordinary share.⁴ ASX was represented by its CEO Robert Elstone, while SGX was led by its CEO Magnus Böcker. Böcker was particularly experienced in exchange mergers. Before his time at the SGX, he had led OMX to merge with a number of other exchanges, including Nasdaq in 2007.⁵ The proposal was for SGX to acquire the shares of ASX Limited, the holding company of the group that ran the securities exchange and conducted all of the clearing and settlement business.⁶ ASX had itself been created by a merger between the Australian Stock Exchange and the Sydney Futures Exchange back in 2006.⁷ In 2010, the market capitalisation was \$1.3 trillion, with the number of listed companies totalling more than 2192.⁸

The merger proposal was attractively packaged around a forecast of profit generating efficiencies. Its rationale was growth, expansion and opportunity. SGX was presented as the gateway to the Asia Pacific markets. Shareholders would receive a substantial premium on

* The author would like to acknowledge, in particular, the assistance of Deborah R. Staines and Sahil Sondhi with this chapter.

¹ *Corporations Act 2001* (Cth) s 411.

² ASX-SGX, 'ASX and SGX Combine to Create the Premier International Exchange in Asia Pacific – The Heart of Global Growth' (Joint News Release, 25 October 2010) 2 <http://www.asx.com.au/documents/media/20101025_asx_sgx_media_release.pdf>.

³ Ibid.

⁴ Ibid.

⁵ Ibid.

⁶ ASX, *The ASX Group* <<http://www.asx.com.au/about/asx-group.htm>>.

⁷ Ibid.

⁸ ASX, 'Annual Report 2010' (Company Report, 2010), 14 <http://www.asx.com.au/documents/media/asx_annual_report_2010.pdf>.

their shares: a 37.3 percent premium.⁹ In addition, there was a lavish hi-tech tempter: the ‘world’s fastest trading platform with the lowest trading latency’ would be built.¹⁰ Technical specifications for this ‘proposed’ platform were not given across any of the public documentation for the merger, although at the time, the SGX platform was said to be superior.¹¹ Under the proposal, the Singapore incorporated ASX-SGX Ltd would be formed, with initial shareholdings of 64% SGX shareholders and 34% ASX shareholders. It would have a primary listing in Singapore and a secondary listing (depositary receipts) on the ASX.

The deal looked to strengthen the size and competitiveness of both ASX and SGX. The merged entity would have a strong presence in the world, especially in Asia Pacific region. Through improving operational efficiencies and savings, the ASX and SGX combined were looking to save \$US30 million per annum in operating costs and offering greater choices to consumers. From the joint media release by ASX and SGX, the new group would be:

- [the] second largest listing venue in Asia Pacific with over 2,700 listed companies from over 20 countries, including over 200 listings from Greater China;
- world’s second largest cluster of companies in the resource sector (more than 900 listings), the largest REITs sector (over 80 listings) and the largest number of ETFs (over 100) in Asia Pacific;
- world’s widest range of Asia Pacific equity, fixed income and commodity derivatives with over 400 contracts from over 10 countries, including Australia, Greater China, India and Japan, and covering a range of commodities including metals, energy and agricultural products; Asia Pacific’s largest and the world’s second largest base of institutional investors with combined assets under management of over US\$2.3 trillion from existing superannuation, institutional and sovereign wealth funds;
- [a] global distribution network with over 90 securities market participant firms and over 170 derivatives market participant firms on a combined basis; and leading

⁹ ASX-SGX, ‘ASX and SGX Combine to Create the Premier International Exchange in Asia Pacific – The Heart of Global Growth’, above n 2.

¹⁰ Ibid 1.

¹¹ Chris Zappone, ‘ASX Launches High-Frequency Trading Platform’, *The Sydney Morning Herald* (online), 28 November 2011 <<http://www.smh.com.au/business/asx-launches-highfrequency-trading-platform-20111127-1o240.html>>. The following year, after the deal had folded, ASX launched its own high frequency trading platform, called *ASX PureMatch*.

exchange technology, including the proposed introduction of the world's fastest trading platform with the lowest trading latency, and flexible data and connectivity solutions.¹²

The ASX-SGX consolidation would have had a positive regional effect, potentially increasing competition of exchanges around the region, and 'bolster the political will of several smaller Southeast Asian exchanges, such as the Bursa Malaysia, the Philippine Stock Exchange and the Stock Exchange of Thailand, to deepen existing ties'.¹³ The Chief Executive of Bursa Malaysia Bhd. Yusli Mohamed Yusoff said that the Malaysian exchange was open to "synergistic opportunities" to work with other exchanges'.¹⁴

In Singapore itself, in reply to parliamentary questions, the Monetary Authority of Singapore (MAS) noted that while the government could not judge the commercial merits of the proposed merger, of which has to be determined by shareholders of the two entities, the transaction has to comply with the *Securities and Futures Act* in Singapore and to satisfy the MAS that the merged exchange would be able to maintain efficient and transparent markets and minimise systemic risks.¹⁵

In Australia, the proposed acquisition faced significant regulatory hurdles. SGX had to seek a clearance from the Australian Competition and Consumer Commission (ACCC) under the *Competition and Consumer Act* (Cth) 2010 ('*the Competition Act*') that the merger posed no anticompetitive risks to the market. The merger needed to be cleared by the Treasurer of the Commonwealth of Australia, Wayne Swan, at the time of the merger, under the *Foreign Acquisitions and Takeovers Act 1975* ('*FATA*') that the merger is not against Australia's national interest.

¹² ASX-SGX, 'ASX and SGX Combine to Create the Premier International Exchange in Asia Pacific – The Heart of Global Growth', above n 2.

¹³ Rebecca Thurlow, Alison Tudor and P R Venkat, 'ASX, Singapore Exchange Face Deal Hurdles', *The Wall Street Journal* (online), 25 October 2010 <<http://www.wsj.com/articles/SB10001424052702304915104575573092152978692>>.

¹⁴ Ibid.

¹⁵ *Securities and Futures Act* (Singapore, cap 289, 2006 rev ed); Monetary Authority of Singapore, *Reply to PQs on Proposed Merger of SGX and ASX*, (22 November 2010) <<http://www.mas.gov.sg/news-and-publications/parliamentary-replies/2010/reply-to-pqs-on-proposed-merger-of-sgx-and-asx.aspx>>.

Further, the *Corporations Act* also imposed a 15% limit on shareholding of the ASX Limited as ASX is a financial market licensee. However, unlike other financial market licensees, the approval mechanism for removing the 15% limit under the *Corporations Act* was not applicable to the acquisition of ASX.¹⁶ Thus, if an investor wanted to obtain more than 15% of shareholding in ASX, the Parliament had to pass a law to remove the 15 percent ownership restriction imposed on ASX under the *Corporations Act* for the deal to go ahead.¹⁷

After all the regulatory approvals from respective authorities, the scheme had to be approved by shareholders of both ASX and SGX.¹⁸ As this was a scheme of arrangement, the scheme ultimately had to be approved by the Federal Court of Australia.¹⁹

The announcement made a start on addressing some of the new corporate arrangements of the merged entity. A holding company would be created, ASX-SGX Limited, which would list on both the Singaporean and Australian exchanges (domiciled in Singapore). The Board would be international, comprised of 15 directors from five countries, including four directors drawn from ASX; the number of directors on the board was later reduced from 15 to 13 and the composition of the board was later amended to have five Australian and five Singaporean citizens, bolstering the appearance of a merger of equals.²⁰ The identities of the CEOs and Directors were set out: Magnus Böcker, current CEO of SGX, would become the CEO of the combined group, and Peter Hiom, the current Deputy CEO of ASX, would become CEO of the ASX business. The parties said they intended these arrangements to be ongoing.²¹

Both exchanges would continue to operate in their own country of origin; or, as one analyst put it '[t]he two exchanges will maintain their current branding, and will be locally regulated and legally distinct'.²² In addition to avoiding the need for regulatory cooperation or

¹⁶ *Corporations Act 2001* (Cth) s 851A.

¹⁷ Monetary Authority of Singapore, above n 15; *Corporation Act 2001* (Cth) pt 7.4, ss 850A, 850B.

¹⁸ ASX-SGX, 'ASX and SGX Combine to Create the Premier International Exchange in Asia Pacific – The Heart of Global Growth', above n 2.

¹⁹ *Ibid.*

²⁰ *Ibid.*

²¹ *Ibid.*

²² Hilary Kincaid, 'ASX to Merge with Singapore Exchange' on LexisNexis, *Corporate Law Blog* (25 October 2010) <<http://www.lexisnexis.com.au/blogs/corporations-law/post/asx-to-merge-with-singapore-exchange.aspx>>.

amendment, this kind of arrangement, common in exchange mergers, does not instil fear into local stakeholders of the possibility of regulatory overspill from another country.

But the optimism of the bid launch ‘minimised the obstacles that needed to be overcome’.²³ Answering questions, Elstone said, ‘We wouldn’t have announced the deal this morning if the boards of both companies didn’t believe it was in the national interests of both countries to form this combination’.²⁴

The problem, immediately apparent to industry watchers, was that SGX’s bid would trigger Australia’s foreign direct investment regime, and the special category reserved for investment by state-owned enterprises of foreign countries, because of the 23% of SGX held, indirectly, by the Singaporean Government.²⁵

Elstone framed the choice as one between domestic confinement and free-wheeling internationalism – appealing to ongoing liberalisation of the economy with a rhetorical question: ‘is the national interest best served by boxing the domestic exchange into its existing strong but confined-to-Australia franchise, or should it allow its domestic exchange to truly internationalize?’²⁶ But there was no getting around the fact that the proposal would be subject to the constraints of Australian law – the *Corporations Act*, limiting ownership in the ASX of a person’s voting power to 15%, and the *FATA*; the former would need special regulatory permission by Parliament, for SGX to succeed in acquiring 100% of the ASX shares.²⁷ The latter could hopefully be flattered, negotiated with, and persuaded. The elusive concept of ‘national interest’ created inherent unpredictability.²⁸

²³ Josephine Coffey, “ASIC’s Forward Agenda” – the Australian Corporate Regulator’s Approach to Timely Disclosure By Listed Companies’ (Paper presented at 2011 SIBR Conference on Interdisciplinary Business & Economics Research: Advancing Knowledge from Interdisciplinary Perspectives, Bangkok, Thailand, 18 June 2011) 2 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1869436>.

²⁴ Thurlow, Tudor and Venkat, above n 13.

²⁵ Matthew Stevens, ‘ASX Takeover’s Success Becomes Matter of Trust’, *The Australian* (online), 26 October 2010 <<http://www.theaustralian.com.au/business/opinion/asx-takeovers-success-becomes-matter-of-trust/story-e6frg9if-1225943436238>>; Coffey, above n 23, 2-3.

²⁶ Thurlow, Tudor and Venkat, above n 13.

²⁷ Vivienne Bath, ‘Foreign Investment, the National Interest and National Security—Foreign Direct Investment in Australia and China’ (2012) 34(5) *Sydney Law Review* 5, 8.

²⁸ Ibid. Bath extrapolates what influences foreign direct investment determinations: ‘domestic policies, manifested through legislation and regulation ... not only the policy of the government of the day towards trade, economic policy and internationalism, but [...also as] political response to pressures from the public, the press, industry associations, competing companies, opposition political parties, regional governments and other groups’.

ASX shareholders were not immediately won over. They possibly thought that ASX was already in a singularly good position without SGX. ASX claimed the largest cluster of resource company listings in Asia Pacific, with some 2000 listings to SGX's 700. Unlike SGX, the ASX had a strong REITs sector, attracting institutional investors. As well, Australia's compulsory superannuation system generated enormous sums of ultimately retail investment in Australian equities. The fact that the ASX was performing well became a major concern for the Treasurer that SGX was obtaining the better part of the deal. Observers said institutional investors sold out of their shares in the ASX when the merger was announced, taking profits as the ASX price rose in the wake of the merger announcement.²⁹

II REACTION TO THE BID

The move by SGX could not have been entirely outside of the realm of speculation by the Australian government. The year before, the government announced that ASIC would become the 'whole-of-market' supervisor of real-time trading in licensed Australian trading markets.³⁰ Responsibility for market surveillance shifted from ASX and others to ASIC in August 2010³¹, concluding a policy shift that saw 'tradition overturned'.³² The Australian Government said that this was 'a necessary step in the process towards considering competition between market operators'.³³ Earlier, it had directly indicated it was open to the idea of the ASX market monopoly being broken. It said it would support competition between exchange markets for trading listed products in Australia.³⁴ It demonstrated this commitment by announcing in-principle support to an Australian market licence for Chi-X

²⁹ Michael Evans and Eric Johnston, 'ASX Merger May Not Make Good Sense, but It Now Looks a Good Bet', *The Sydney Morning Herald* (online), 12 February 2011 <<http://www.smh.com.au/business/asx-merger-may-not-make-good-sense-but-it-now-looks-a-good-bet-20110211-1aqp7.html>>, '... big ASX shareholders sold into a sharp rise in the share price after the SGX deal was announced, not wanting to be left holding shares in the combined exchange', 'ASX merger may not make good sense, but it now looks a good bet'.

³⁰ Chris Bowen and Wayne Swan, 'Reforms to the Supervision of Australia's Financial Markets' (Joint Media Release, No 013, 24 August 2009) <<http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/013.htm&paragraphsID=003&min=ceba&Year=2009&DocType=0>>.

³¹ Australian Securities & Investments Commission, *Supervision* <<http://asic.gov.au/regulatory-resources/markets/supervision/>>.

³² Coffey, above n 23, 3. 'The nineteenth century established that the relationship between a stock exchange and its listed companies, and between the stock exchange and its member brokers, was regulated by the terms of a common law contract with its associated rights and obligations. In Australia, this system was encapsulated in the ASX rules. This tradition was overturned in 2010...'.

³³ Australian Securities & Investments Commission, 'Australian Equity Market Structure: Proposals' (Consultation Paper No 145, Australian Securities & Investments Commission, November 2010). <<http://download.asic.gov.au/media/1329506/cp-145.pdf>>.

³⁴ Ibid.

Australia Pty Limited (CXA).³⁵ In fact, several operators had at one time made applications for the crucial licence, regulated by the *Corporations Act*,³⁶ but by then only Chi-X was still in the game.³⁷ The Australian Securities and Investments Commission (ASIC) stated that it was a ‘significant milestone for Australian equity markets’, conforming to the policy of bringing competition between exchange markets to Australia.³⁸

Stock exchanges, however, are national signifiers, creating resistance to consolidation and loss of identity, to say nothing of possible loss of regulatory control. Unlike Europe, Australia was not part of a multi-lateral inter-state superstructure, and had little familiarity with these kinds of arrangements. In addition, a stock exchange has practical, material value as well as being symbolic – it provides a gateway to capital raising, it creates jobs in the finance sector, it opens its door to local companies. However, part of the difficulty in the merger proposal may have been that SGX and ASX, by this dramatic reconfiguration, were overtaxing the capacity for governmental policy and regulation to adapt to new circumstances.

Expert evaluation saw both strengths and weaknesses in the proposal. Many thought the initial board structure was unbalanced (and indeed, was later amended).³⁹ The Singapore Government was a major shareholder in SGX, owning 23%, but was said that to consider reducing that position to below the Australian 15% threshold. One commentator noted that such a significant holding by the Singapore Government could result in pressure by it being exerted on the holding company, impacting the credibility and integrity of the product offered by the exchanges.⁴⁰ As a counter, others contended that ‘SGX would be committing financial suicide to pay the sort of premiums it plans to (37 per cent over the pre-trading halt price, 47 per cent over the three-month volume-weighted average price and 45 per cent over the six-month VWAP) if it then went about undermining the credibility and integrity of its product’⁴¹

³⁵ Chris Bowen, ‘Government Announces Competition in Financial Markets’ (Media Release, No 032, 31 March 2010) <<http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2010/032.htm&pageID=003&min=ceba&Year=&DocType=0>>.

³⁶ *Corporations Act 2001* (Cth).

³⁷ Australian Securities & Investments Commission, ‘Australian Equity Market Structure: Proposals’, above n 33.

³⁸ Coffey, above n 23, 2, citing Australian Securities & Investments Commission, ‘ASIC Publishes Chi-X Licence’ (Press Release, 89AD, 4 May 2011) 11; ‘ASIC Publishes Final Competition Market Integrity Rules’ (Press Release, 87MR, 29 April 2011) 11.

³⁹ Evans and Johnston, above n 29.

⁴⁰ Stevens, above n 25.

⁴¹ Ibid.

Given the limited depth and liquidity of Australian capital markets compared to other world markets, the offshore participation that a merger with SGX would bring was enticing.⁴² One commentator acknowledged the attractive potential of the proposed merger, which would include benefits to GDP of Australia because of off-shore participation in Australian capital markets, and employment growth in financial services because of a higher volume of transactions flowing through.⁴³

However, the same commentator warned that it was always possible that these jobs could be ‘rationalised’ away from Australia.⁴⁴ He noted that this potential outcome was not usually raised as an issue with ‘overseas exchange mergers or takeovers as the clearing entities tend to be separated from the exchanges’.⁴⁵ In Australia, these roles were not separated, despite the changes which had been undertaken since 2010, involving handing over of regulatory power by ASX to ASIC and the opening up of the Australian monopoly to competition. Hosking hinted that perhaps more beneficial arrangements in terms of ongoing sector growth (jobs) could be flow from cooperation with parties other than SGX. Some thought that ‘Singapore needs the merger more than the ASX’ and suggested ASX look to partner with Hong Kong or, an even more unlikely scenario, an exchange within mainland China.⁴⁶ Others said that SGX had gotten off on the wrong foot, and needed to reconceive the bid as a ‘merger of equals’ similar to the model adopted by LSE and Toronto to make it politically palatable.⁴⁷ The ‘merger of equals’ card has played out differently in different situations; it did not outweigh nationalist concerns in the failed London/Toronto merger but was more successfully invoked, at least initially, in the case of Euronext and NYSE. Even there, however, winning over recalcitrant shareholders, political actors and regulators took some doing.

A week after the October 2010 announcement, ASX issued a Companies Update stating that ASX viewed the proposal as a ‘natural next stage in the evolution of Australia’s capital

⁴² Les Hosking, ‘Weighing Up an ASX-SGX Merger’ (2011) 125(1) *inFinance* 38, 38-39.

⁴³ Ibid.

⁴⁴ Ibid.

⁴⁵ Ibid.

⁴⁶ Evans and Johnston, above n 29.

⁴⁷ Ibid.

markets’.⁴⁸ The first paragraph argued that the merger would ensure ‘Australia’s ongoing relevance in the global marketplace’. Relevance was a theme repeated by Mr Böcker at the merger announcement and reported in the press.⁴⁹ This was eagerly repeated by some.⁵⁰

Whilst there clearly was government support for opening up the continent to international capital markets, the relevancy argument implied that ASX was the weaker (more irrelevant) entity. This dismissal was picked up upon by Treasurer Swan, further down the track. It should be noted that ASX maintains that ‘[i]n the five years from 2009 to 2013, ASX ranked in the top five exchanges globally for total equity capital raised by listed issuers’.⁵¹ But in 2010, stock exchange consolidation was the buzz, it was happening. Would Australia defy the trend and remain a national enterprise or would this proposal change everything?

The update also disclosed to the market some particulars about the proposal not covered earlier, regarding regulation, liquidity, and access issues. If the merger went ahead, ‘all existing protections around ASX’s listing rules and corporate governance standards’ would be preserved.⁵² The *Corporations Act* would remain applicable to all registered companies in Australia. ASIC would continue to perform the regulatory role for the exchange arm of ASX in Australia and the Reserve Bank of Australia would be responsible for regulating the clearing and settlement arm of ASX. The Corporate Governance Council of ASX would continue to develop and recommend better corporate governance practices to be adopted by ASX listed entities.

Technically, there was no real doubt about who would regulate the exchange business in Australia, but later events would show that the clearing and settlement role of the ASX was pivotal to the government’s view of the proposal. The update also stressed that existing

⁴⁸ ASX, ‘ASX Limited Merger Implementation Agreement with Singapore Exchange Limited’ (Companies Update No 10/10, 4 November 2010) <http://www.asx.com.au/resources/newsletters/companies_update/archive/CompaniesUpdate_20101101_1010_HTML.htm>.

⁴⁹ Thurlow, Tudor and Venkat, above n 13. ‘This is a question of not only creating new opportunities for existing customers, it’s a question of staying relevant in a rapidly changing market,’ Mr. Bocker said, ‘ASX, Singapore exchange face deal hurdles’.

⁵⁰ Maurice Newman, ‘Say Yes to Singapore Merger or Risk Irrelevance’, *The Australian*, 27 January 2011.

⁵¹ ASX, *Capital Raising* <<http://www.asx.com.au/listings/capital-raising.htm>>.

⁵² ASX, ‘ASX Limited Merger Implementation Agreement with Singapore Exchange Limited’, above n 48.

business relations between ASX Issuers department and listed entities would be maintained, to facilitate listing compliance.

The update outlined how they would approach the main hurdle – getting approval from the Foreign Investment Review Board. This application, as it was stated, would frame the benefits of the merger including: ‘increased profile and visibility among the global investment community; access to the largest institutional investor base in the Asia-Pacific region; and potential lower costs of capital as a result of enhanced liquidity’.⁵³

The chairperson of the ASX Ltd Board, David Gonski, sent the formal letter of Board approval of the deal to shareholders in early December 2010, saying that, while the proposal was subject to various approval processes, including a parliamentary process to lift ownership restrictions on the ASX (in reference to ownership constraints in the *Corporations Act/ Financial Sector (Shareholdings) Act 1998*), the Board was unanimous in recommending the transaction to shareholders.⁵⁴ The letter also advised all shareholders that the Board had engaged Access Economics (now Access Economics Deloitte, describing itself as an economics advisory practice) to examine the ‘national interest implications’ (a reference to the FIRB hurdle).

The *Access Economics* assessment of the merger was positive.⁵⁵ The report concluded that the merger was likely to advance the national interest of Australia.

[T]he formation of ASX-SGX would promote Australia’s national interest since it is highly likely to raise the economic welfare of Australians by:

- improving Australia’s chances of becoming a financial services hub in Asia;
- improving the ability of Australians to diversify their savings; and
- lowering the cost of capital for Australian companies.⁵⁶

⁵³ Ibid.

⁵⁴ Letter from David Gonski, ASX Chairman, Sydney, to ASX Shareholders, 6 December 2010, <http://www.asx.com.au/documents/media/101206Shareholder_Letter_-_ASX-SGX_Merger_Proposal.pdf>.

⁵⁵ ASX Group, ‘Access Economics Report on ASX-SGX Combination’ (Media Release, 6 December 2010) <http://www.asx.com.au/documents/media/101206Launch_of_Access_Economics_Report_on_ASX-SGX_Final.pdf>.

⁵⁶ Ibid.

The report further stated that the merger was not contrary to Australia's national interest given the operation of ASX would remain in Australia and be subjected to Australian regulatory authorities.

III COMPETITION REGULATOR APPROVAL OF THE BID

The deal received approval from the Australian competition regulator –ACCC. The ACCC is the national regulator responsible for assessing proposed mergers on anti-competitive (antitrust) issues. The Commission commented very early on the deal that it sought 'real competition for stock market trading in Australia',⁵⁷ followed by an informal review conducted on the proposal.⁵⁸

The ACCC applies the *Competition Act* to examine issues relating to mergers and acquisitions.⁵⁹ The relevant section of the *Act* is s 50 which prohibits acquisitions that would result in a substantial lessening of competition in the relevant market. If a merger is deemed to have the effect of substantial lessening of competition in the relevant market, the Commission can block the merger by refusing to grant a clearance.⁶⁰ The prohibition is guided by s 50(3) which provides a list of factors that must be taken into account, including levels of import competition; levels of concentration in the market; and, at s 50(3)(f), 'the extent to which substitutes are available in the market...'.⁶¹ It is very interesting to note that under s 50(3)(i), of the *Competition Act* the Commission has to take into account specifically 'the nature and extent of vertical integration in the market'.⁶² Given the structure of ASX Limited, which has a vertically integrated business structure, it was cleared by the ACCC that it posed little competition risk to the Australian market. However, the business structure of ASX Limited became a substantial factor for FIRB to determine that the deal was not in the national interest of Australia.

⁵⁷ Reuters, 'ASX Takeover Not a Competition Issue: Graeme Samuel', *The Sydney Morning Herald* (online), 25 October 2010 <<http://www.smh.com.au/business/asx-takeover-not-a-competition-issue-graeme-samuel-20101024-16zoi.html>>.

⁵⁸ ACCC, *Singapore Exchange Limited – Proposed Acquisition of ASX Limited* (15 December 2010) <<http://registers.accc.gov.au/content/index.phtml/itemId/962036>>.

⁵⁹ *Competition Act 2010* (Cth), s 50.

⁶⁰ *Ibid* ss 95AF, 95AM(1).

⁶¹ *Ibid* s 50(3)(f).

⁶² *Ibid* s 50(3)(i).

Enhanced criteria for merger assessments are provided in the ACCC's '*Merger Guidelines*', an internal policy document available from its website.⁶³ They elaborate on the factorial analysis decreed in statute, and also allude to other unspecified but 'relevant factors that may pertain to the ACCC's approach to s 50'.⁶⁴ The Foreword explains that it is an approach that offers 'an increased emphasis on the competitive theories of harm and the effect of constraints, which facilitates a more integrated analysis'.⁶⁵ In the event, the ACCC approved the merger, concluding that 'the proposed acquisition was unlikely to result in a substantial lessening of competition in the relevant markets'.⁶⁶ It found that while ASX and SGX do compete for listing services – a level of competition that could be lost through merger – they only did so to a limited extent; and that in Australia, SGX did not compete with ASX for trading, clearing or settlement services.⁶⁷

Its main concern seemed to be whether the new entity would be too big – would the proposed acquisition 'deter the entry' of other market players into Australia? If it did, that might leave the new ASX-SGX with a monopoly. As the existing ASX already held a monopoly over trading in the traditional public (or 'lit') markets, this was something of a moot point. But the Australian Government was encouraging other players to enter the field, and the analysis had to consider if they would be deterred. To explore this possibility, the ACCC's attention turned to Chi-X Global (CXG), known to be planning two operations within the country – one lit (Chi-X Australia Pty Ltd [CXA]) and one dark venue (Chi-East). The complicating factor was that SGX was in a 50-50 joint venture with Chi-X Global for the dark Chi-East operation.

The ACCC determined, firstly, that SGX had no economic interest in CXG, so the proposed ASX-SGX merger 'would not alter CXA's incentives'. In fact, the SGX-ASX merger may have been prompted by the plans for CXA to enter Australia. At the merger announcement,

⁶³ ACCC, *Merger Guidelines* (2008) <<https://www.accc.gov.au/publications/merger-guidelines>>.

⁶⁴ ACCC, *Informal Merger Review Process Guidelines* (2013) <<https://www.accc.gov.au/publications/informal-merger-review-process-guidelines-2013/informal-merger-review-process-guidelines-2013/1introduction/section-50-of-the-act>> ('*Informal Merger Review Process Guidelines*'); See also, ACCC, *Merger Guidelines* (2008), above n 63. As explained at 1.15 of the Informal Merger Review Process Guidelines, the ACCC's approach to the merger factors is set out in the Guidelines (esp. chapter 7 of the Merger Guidelines), and 'other factors not listed in s. 50 may also be relevant to a merger assessment.

⁶⁵ ACCC, *Merger Guidelines* (2008), above n 63, 1.

⁶⁶ ACCC, *Singapore Exchange Limited – Proposed Acquisition of ASX Limited*, above n 58.

⁶⁷ Ibid.

ASX CEO Robert Elstone agreed that it was a factor.⁶⁸ The *Sydney Morning Herald* interpreted the interest of ASX in the merger as a defensive strategy; the ASX would lose its domestic monopoly with the impending entry of CXA. By merging with SGX, the ASX might ‘ward off the threat of alternative trading systems’.⁶⁹

Secondly, the ACCC considered whether the proposed merger would impact on the nascent dark pool venture, Chi-East. It considered that SGX’s 50% ownership in Chi-East might alter the economic incentives of Chi-East to compete with the new super entity. However, it concluded that the extent to which Chi-East and the ASX would actually compete for dark pool trading services would be fairly limited.⁷⁰ In fact, Chi-East closed within 2 years of beginning operations in Australia, due to disappointing trading volumes. On the other hand, Chi-X Australia, the lit venue, continues to operate.⁷¹

Non-Australian competition regulators have subsequently not been as sanguine about stock exchange consolidation as Australia’s. When ICE and Nasdaq threatened to bid for a combined NYSE Euronext-Deutsche Bourse in 2011, the US Justice Department said ‘No’.⁷² The EC blocked the Deutsche aspect of this mega-merger in 2012. Both these proposed mergers were found to be anti-competitive.⁷³

IV THE TREASURER REJECTS THE BID

Between December 2010 and February 2011, the upbeat sentiments of the ASX gave way to the realities of the regulatory and political hurdles ahead. On February 15, 2011, SGX announced a change in board composition for the merged entity, providing for an equal number of ASX and SGX directors.⁷⁴ Shortly afterwards, on March 11, 2011, the ASX

⁶⁸ Evans and Johnston, above n 29, quoting Elstone at a merger announcement ‘It was a game changer because it clearly signalled the government’s relaxed nature about wholly owned foreign companies competing against us’.

⁶⁹ Reuters, ‘ASX Takeover Not a Competition Issue: Graeme Samuel’, above n 57.

⁷⁰ ACCC, *Singapore Exchange Limited – Proposed Acquisition of ASX Limited*, above n 58.

⁷¹ Eleni Himaras, ‘Chi-East to Close Operations after Disappointing Volumes,’ *Bloomberg* (online), 11 May 2012 <<http://www.bloomberg.com/news/articles/2012-05-10/chi-east-to-close-operations-after-disappointing-volumes>>.

⁷² Lauren Pollock, ‘Nasdaq, ICE Withdraw Bid for NYSE after DOJ Talks,’ *MarketWatch* (online), 16 May 2011 <<http://www.marketwatch.com/story/nasdaq-ice-withdraw-bid-for-nyse-after-doj-talks-2011-05-16-89590>>.

⁷³ But both of those decisions came after the ASX-SGX merger had been scuttled.

⁷⁴ ASX, Market Announcement, ‘New ASX-SGX Governance Arrangements and Commitments to Strengthen the Merger Proposal’ (Joint News Release, 15 February 2011) <http://www.asx.com.au/documents/media/20110215_asxsgxjointnewsrelease.pdf>; Reportedly, ‘SGX and ASX had replied to more than 100 queries from the regulator relating to their merger proposal, sources with knowledge of the

announced that the SGX had formally lodged its FIRB application respecting the proposed merger.⁷⁵ ASX noted that the two companies had amended their original MIA as well, to reflect the new board composition announced in February.⁷⁶

In addition to the competition clearance required for the merger, the ASX and SGX merger was subject to the Australia's foreign investment framework, or *FATA* (the *Foreign Acquisitions and Takeovers Regulations 1989 (the Regulations)*, the *Foreign Acquisitions and Takeovers (Notices) Regulations 1975* and the Australia's Foreign Investment Policy).⁷⁷ The application of the framework was triggered, in particular, because the SGX was a foreign government investor as the Singaporean Government indirectly owned more than 15 percent of the SGX.⁷⁸ Regardless of the value of the investment, SGX had to make an application to the FIRB.⁷⁹

Under the Framework, the review of proposed acquisitions involves the FIRB and the Treasurer of the Commonwealth Government of Australia. The FIRB is responsible for reviewing the applications by foreign entities and providing advice to the Treasurer about the proposed acquisitions.⁸⁰ Upon the advice provided by the FIRB, the Treasurer can exercise his or her power, under the *FATA*, to determine whether the foreign investment is contrary to the national interest and make the decision to accept or reject applications, or to impose certain conditions on foreign investments.⁸¹

One of the most important aspects of the *FATA* framework is the national interest requirement, which, unfortunately, is not defined. However, following Senate's scrutiny of foreign investment, the FIRB had published and released a newer version of Australia's Foreign Investment Policy on 30 June 2010, providing a more detailed description of the

deal said', Reuters, 'How the ASX-SGX Merger Failed', *The Sydney Morning Herald (online)*, 21 April 2011 <<http://www.smh.com.au/business/how-the-asxsgx-merger-failed-20110421-1dqb2.html>>.

⁷⁵ ASX, Market Announcement, 'ASX-SGX Merger Proposal Application Lodged with FIRB' (Media Release, 11 March 2011) <http://www.asx.com.au/documents/media/110318_ASXSGX_Merger_application_Lodged_FIRB.pdf>.

⁷⁶ Ibid.

⁷⁷ Foreign Investment Review Board, *Guidance Note 1 - Australia's Foreign Investment Framework* (February 2012) <http://www.firb.gov.au/content/guidance/downloads/gn1_jan2012.pdf>.

⁷⁸ Ibid.

⁷⁹ ASX, Market Announcement, 'ASX-SGX Merger Proposal Application Lodged with FIRB', above n 75.

⁸⁰ Foreign Investment Review Board, above n 77.

⁸¹ Ibid.

factors used to assess the national interest of proposed acquisitions.⁸² Factors to be considered by FIRB include national security, competition, tax revenues and other Australian Government policies.⁸³

Community concerns about foreign ownership of certain Australian assets also play a role,⁸⁴ as well as the nature of the investor, for example, foreign government investors.⁸⁵ At the time of the bid, some 23% of SGX was owned by SEL Holdings, in turn 100% owned by Temasek Holdings, in turn 100% owned by the Singapore government.⁸⁶ SGX's tactics, if not its entire strategy, should have turned on this fact, as 'the Australian Government...considers if the investment is commercial in nature or if the investor may be pursuing broader political or strategic objectives that may be contrary to Australia's national interest. This includes assessing whether the prospective investor's governance arrangements could facilitate actual or potential control by a foreign government (including through the investor's funding arrangements)'.

As we now know, the FIRB recommended to the Treasurer on April 2, 2011 that the SGX bid should not be approved.⁸⁷ On April 5, 2011, SGX was notified by the FIRB that Treasurer

⁸² John Reen, *New Australian Foreign Investment Policy* (14 July 2010) Dibbs Barker <http://www.dibbsbarker.com/publication/New_Australian_Foreign_Investment_Policy.aspx>.

⁸³ Ibid.

⁸⁴ Senate Standing Committees on Rural and Regional Affairs and Transport, Parliament of Australia, *Foreign Investment and the National Interest* (2013) xi <http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Rural_and_Regional_Affairs_and_Transport/Completed%20inquiries/2012-13/firb2011/report/b02>. Sometime after the SGX bid, and in response to different concerns about 'selling the farm', an inquiry into the FIRB and national interest test was launched but it merely resulted in recommendations to further strengthen the national interest test, including the provision of unambiguous instructions to prospective investors on their *obligations* under FIRB.

⁸⁵ The Government would have treated SGX as a not-wholly foreign government owned investor (another name for this is 'government-linked company', or GLC), the policy requiring it therefore to take into account the size, nature and composition of any non-government interests, including any restrictions on the exercise of their rights as interest holders, and the bid could look to some mitigating factors on its side – the existence of external shareholders, and ASX remaining on the Australian social exchange. However it is unclear whether the governance arrangements were satisfactory.

⁸⁶ Singapore Exchange Limited, 'SGX The Asian Gateway: Singapore Exchange Annual Report 2011' (Company Report, 30 June 2011) 9, Figure 3: SGX Shareholders on 30 June 2011 Another 41% was owned by Institutions, of which 35% were Singapore based, Figure 4: SGX Institutional Shareholders by Geography.

⁸⁷ Foreign Investment Review Board, 'Singapore Exchange Limited - Acquisition of ASX Limited', (Minute, F2011/01924, 2 April 2011) 1, FIRB applications are generally treated as commercial in confidence and not usually released. We located these documents, which were released by the Foreign Investment Review Board under the Freedom of Information Act, on the Treasury website. The statement says that they were released under an FOI request 'for advice given to the government by FIRB about the Singapore Exchange merger proposal with the ASX.' The advisories from RBA and ASIC that were mentioned in the FIRB minute were not publicly released and are not available on neither ASIC disclosure log table, <<http://asic.gov.au/about-asic/freedom-of-information-foi/foi-disclosure-log/freedom-of-information-asic-disclosure-log-table/>>, nor the RBA Freedom of Information Disclosure Log, <<http://www.rba.gov.au/foi/disclosure-log/>>.

Swan was disposed to reject the proposed merger on national interest grounds.⁸⁸ The ASX issued a market announcement on the Treasurer's decision and promptly saw its share price drop, closing 3.3% lower.⁸⁹ Although still unofficial, that day's headline in the *Sydney Morning Herald* read 'Swan rejects ASX takeover'.⁹⁰ SGX responded with a press conference on April 5, 2011. Böcker stated simply that they had no plans to amend their proposal.⁹¹

The SGX did, however, later further substantiate its proposed acquisition; the second Minute (April 7, 2011) released by FIRB stated that SGX 'provided a further submission to Treasury on April 7, 2011 in support of its proposed acquisition of ASX Limited'.⁹² The new submission was considered by FIRB, the RBA and the ASIC and subsequently dismissed by all three authorities.⁹³ On April 8, 2011, the Treasurer formally announced that he would not be approving the merger bid, on the grounds of it being contrary to the national interest.⁹⁴

My decision was based on unambiguous and unanimous advice from FIRB that the proposed transaction was contrary to the national interest. I have also drawn on a broad range of stakeholder perspectives in the five months since the transaction was publicly announced in October 2010.⁹⁵

The Treasurer was required to give reasons under the *FATA*.⁹⁶ He said it was in the national interest to maintain the strength and stability of the Australian financial system, and to continue building Australia's standing as a global financial services centre in Asia, for the

⁸⁸ ASX, 'Treasurer Disposed to Reject ASX-SGX Merger Proposal' (Media Releases, 5 April 2011) <http://www.asx.com.au/documents/investor-relations/110405_asx_firb_treasurer.pdf>.

⁸⁹ Eric Johnston, 'Swan Rejects ASX Takeover', *The Sydney Morning Herald* (online), 5 April 2011 <<http://www.smh.com.au/business/swan-rejects-asx-takeover-20110405-1d25e.html>>.

⁹⁰ Ibid.

⁹¹ Chris V Nicholson, 'Regulators Set to Reject Merger of Singapore and Australia Exchanges', *The New York Times* (online), 5 April 2011 <http://dealbook.nytimes.com/2011/04/05/australia-says-its-set-to-reject-sgx-asx-merger/?_r=0>.

⁹² Foreign Investment Review Board, 'Singapore Exchange Limited - Acquisition of ASX Limited', (Minute, F2011/01924, 7 April 2011) 1, this minute does not cite the national security exemption under FOI (s. 33), as in the minute dated 2 April 2011 on the same matter, but does cite the exemption provisions for material obtained in confidence, deliberative processes, and other conditionally exempt sections.

⁹³ Ibid.

⁹⁴ Wayne Swan, 'Foreign Investment Decision' (Media Release No 030, 8 April 2011) <<http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2011/030.htm&pageID=003&min=wms&Year=2011&DocType=0>>.

⁹⁵ Ibid.

⁹⁶ Under the *FOI Act*, Swan's official decision should be available: '(c) the record of, or a formal statement of the reasons for, a final decision given in the exercise of a power or of an adjudicative function.' *Freedom of Information Act 1982* (Cth), s 47C(3).

benefit of the invested superannuation savings – and that he had concerns that the acquisition would be contrary to those objectives.

For Swan, selling the exchange was not simply a question about pricing a major piece of infrastructure. He had to look beyond both the commercial impact of the transaction and the maintenance of the regulatory perimeter – questions which were complex but measurable – and consider the national interest.

He said that the proposal would result in a loss of sovereignty – specifically, of ‘economic and regulatory sovereignty’, which are different things. Loss of regulatory sovereignty was a weak point in the argument, to the extent that ASX was to remain in Australia, subject to Australian regulatory oversight. But the issue of economic sovereignty is a little different. The ASX was no longer state owned, so the government had no day-to-day control over its activities in the classic sense of economic sovereignty; sale of ASX however could possibly remove any remnant of Australian government intervention in its operations. The Treasurer then recited the somewhat vague objectives he wished to promote: integrity of the financial architecture and regulatory framework, growing the access to global capital markets and exchange networks, sector employment growth, and increasing competition.

Not everyone was persuaded by the Treasurer’s reasoning. Frino, writing after the merger had been disallowed, questioned the impingement on regulatory sovereignty; in his view, an important opportunity had been passed up. SGX had demonstrably attracted an international order flow in comparison with the ASX, which tended to rely on soaking up domestic capital and superannuation savings.⁹⁷ The merger, he said, would have enabled Australia to better tap global capital markets.⁹⁸ Referring to the deals then on the table between the London Stock Exchange and the Toronto Stock Exchange, and between NYSE Euronext and Deutsche Bourse, Frino argued that the Treasurer’s rejection was ‘contrary to what is happening globally’.⁹⁹ With hindsight, we can see that the Australian decision against

⁹⁷ Alex Frino, ‘Knocking Back the ASX-SGX Merger Will Hurt Australia’, *The Conversation* (online), 8 April 2011 <<http://theconversation.com/knocking-back-the-asx-sgx-merger-will-hurt-australia-693>>, Australia has the fourth largest pension fund market in the world.

⁹⁸ Ibid.

⁹⁹ Ibid.

consolidation anticipated the end of this wave of exchange consolidations – the above named deals fell through. Other critics deplored the secrecy of the discretionary process.¹⁰⁰

However, the cool reception given to the bid in Canberra appeared to reflect a more widely-held view. Austin perceived both political and commercial opposition to the bid, in particular to the lack of equal board representation at the proposed new entity, and crystallising around the idea of a takeover of a national infrastructure.¹⁰¹ Industry players thought the inevitable result would be a shift offshore of the financial sector's power base, and with it, domestic employment prospects. Despite the rhetoric, some industry participants did not see actual Asian engagement with Australia resulting.¹⁰² Austin concluded that, aside from all of the real-political issues, a major strategic weakness of the proposed merger was the 'negligible' diplomacy (networking) with federal parliament beforehand, which he attributes to Bocker and SGX as the leads on the acquisition.¹⁰³ Indeed, one of the indirect consequences of the merger not going ahead as planned was that SGX CEO Bocker stepped down from his role, being described, fairly or not, as the 'man who failed'.¹⁰⁴ The *New York Times* had already declared the merger as 'a value-destructive move' – if it passed.¹⁰⁵

V LESSONS ON 'THE NATIONAL INTEREST' TEST

Since the 1970s, there has been an increasing liberalisation of Australia's foreign investment policy through the introduction of higher thresholds, and the progressive loosening of equity and control requirements. The *FATA* introduced a regime for screening and authorising business, investment and purchases.¹⁰⁶ FIRB was established in 1976, to include independent

¹⁰⁰ Megan Bowman, George Gilligan and Justin O'Brien, 'Foreign Investment Law and Policy in Australia: A Critical Analysis' (2014) 8(1) *Law and Financial Markets Review* 65, '[L]ittle information is released about how such decisions are constructed,'; Reuters, 'How the ASX-SGX Merger Failed', above n 74, Sydney University Economics and Business School Professor Alex Frino said 'I think there should be more transparency on how the decision was reached. I think that would be in the national interest'.

¹⁰¹ Ian Austin and Simon Minaee, 'The Proposed ASX-SGX Merger - An Australian Perspective' in Ian Patrick Austin (ed), *Australia-Singapore Relations: Successful Bilateral Relations in a Historical and Contemporary Context* (Select Publishing, 2011) 221, 225.

¹⁰² Malcolm McComas and Brad Orgill, 'If Not the Banks, Why the Exchange?' *Australian Financial Review*, 1 November 2010, 55 cited in Austin and Minaee, above n 101, 228.

¹⁰³ Austin and Minaee, above n 101, 221.

¹⁰⁴ Will Hadfield and Jonathan Burgos, 'Singapore Exchange CEO Who Failed to Acquire ASX Steps Down', 24 February 2015 <<http://www.bloomberg.com/news/articles/2015-02-24/singapore-exchange-s-chief-executive-bocker-to-step-down-in-june>>.

¹⁰⁵ Rob Cox and Wei Gu, 'Silver Lining in FDIC Deal', *The New York Times* (online), 25 October 2010 <<http://www.nytimes.com/2010/10/26/business/26views.html?emc=tnt&ntemail0=y&r=0>>.

¹⁰⁶ Senate Economics References Committee, The Parliament of Australia, *Foreign Investment by State-owned Entities*, (2009) 3.5-3.8.

panel members to give expert advice to Treasury from people reflecting community and commercial perspectives.¹⁰⁷ In 1976, the ‘national interest’ test was introduced, a concept ‘created by legislation and elaborated on by the issue of various guidelines and policies which constitute Australia’s foreign investment system’.¹⁰⁸ An important policy reference point for Treasurer Swan would have been the Senate Economics References Committee *Report on Foreign Investment by State Owned Entities* (2009), which addressed many of the key issues head on.¹⁰⁹ The Committee view, at 3.42, is that it considers ‘the chief virtue of the national interest test is its flexibility. Its unwritten or undefined character—the fact that it is a negative test—enables it to adapt more easily to changing circumstance. A prescriptive test with specific criteria would not allow this degree of flexibility’.¹¹⁰ Further, it concluded that it was justified for the government to continue to treat applications for investment by state-owned enterprises (SOEs) as a special category because ‘their interests may not be simply commercial’. Although SGX allegedly deployed lobbyists to Canberra¹¹¹ (apparently after announcing the bid), SGX and ASX may have underestimated the importance of convincing the relevant agencies, departments and politicians of the positive aspects of the proposed merger. As ‘each proposal is assessed individually and the standard for review in all cases is whether the transaction would be contrary to the national interest, as determined by the Treasurer,’¹¹² marshalling the facts is an important aspect of the process.

Appearing before *Senate Economics Legislation Committee* some weeks after the rejection was announced, FIRB had the opportunity to explain its reasoning further.¹¹³ The Committee was especially interested in the question of national interest. Senator Helen Coonan (Liberal Party), former government minister, observed that there were lessons to be learned from the trajectory of this bid.¹¹⁴ Responding to her questions, FIRB acknowledged that the vertically integrated monopoly on settlement and clearing had been a stumbling block to the merger.¹¹⁵ FIRB’s Jim Murphy, executive director of FIRB’s ‘Markets’ section, reported that both the

¹⁰⁷ Ibid.

¹⁰⁸ Bath, above n 27, 6.

¹⁰⁹ Senate Economics References Committee, above n 106.

¹¹⁰ Ibid 30 [3.42].

¹¹¹ Reuters, ‘How the ASX-SGX Merger Failed’, above n 74.

¹¹² Bath, above n 27, 8.

¹¹³ Commonwealth, *Parliamentary Debates*, Senate, 1 June 2011, 77-84.

¹¹⁴ Ibid 78.

¹¹⁵ Ibid.

RBA and ASIC had identified potential systemic risks to the Australian financial system if ASX's settlement and clearing business were to be controlled by other foreign entities, despite Australian regulatory oversight..¹¹⁶ In response to one of the committee members' question on whether separating the settlement and clearance arm from the rest of the business would have made the merger likely to be approved, Mr Murphy implied that there may have been ways to re-organise the entities to be more merger-friendly, but he didn't think SGX-ASX has done that.¹¹⁷

FIRB then stated there was more than one fundamental issue with the SGX bid under the banner of 'national interest' which could not be disposed of.¹¹⁸ Coonan homed in on the key problem: what to do about bids that transferred ownership to entities 'with competing national interests'?¹¹⁹ The senator was interested in whether the outcome of the SGX-ASX merger talks indicated a need for greater clarity about the different factors weighed in the 'national interest', for the purpose of signalling requirements to future investors. The scope for national interest is multifactorial, and perhaps daunting for newcomers. Bath observed that the OECD had criticised the Australian national interest test, as well as from the usual 'small government' proponents.¹²⁰ On the one hand, refusal to approve the merger can be seen as as a classic case of 'arbitrary' decision-making; on the other, it was, at the time, widely supported in Australia. Allegations of abuse of executive power were not raised and the 'policies have clearly not deterred foreign investment'.¹²¹

Further, Australia and Singapore have long-held generous and broad commercial ties. Australia has been a party to a free trade agreement with Singapore since 2003.¹²² Austin observed that the relationship between the two countries is a positive one, characterised by a 'general lack of tension and conflict,' with an ongoing depth of commercial, political, and

¹¹⁶ Ibid 77. The ASX's structure can be contrasted and compared with other countries where the main trading platform and the clearance and settlement systems operate as separate entities. Mr Murphy said that the FIRB established a new government-supported working party to consider what powers the Australian regulators would need to hold to prevent this factor being an impediment to future merger proposals.

¹¹⁷ Ibid 78.

¹¹⁸ Ibid.

¹¹⁹ Ibid.

¹²⁰ Bath, above n 27, 17.

¹²¹ Ibid.

¹²² *Singapore–Australia Free Trade Agreement*, signed 17 February 2003, [2003] ATS 16 (entered into force 28 July 2003).

cultural exchange.¹²³ Although hiccups or surprises may not be uncommon, with errors on both sides, political pragmatism dominates the relationship¹²⁴, and the mutual benefits for regional security are regularly reinforced at the ASEAN summit.¹²⁵ The case for the merger would have benefited, according to Austin, from the existing good feeling between the two nations and it is undeniable that ‘Australia has long been an open recipient of Singaporean investment’.¹²⁶ Indeed, when it comes to foreign investment protocols, Singapore has an advantage over everybody else – it receives its own specialised help-desk at the FIRB.¹²⁷ And many ‘Singaporean government-linked enterprises (GLCs) own major Australian infrastructure’.¹²⁸

However, although Singapore is technically a parliamentary republic with a Westminster system of parliamentary governance, it is widely perceived as only a ‘hybrid regime’, not having attained full democracy in practice.¹²⁹ Despite these question marks, there is no denying that at the time of the bid, Singapore was rated as a very competitive and business-friendly environment, strong on institutions, infrastructure, and macroeconomic environment,¹³⁰ and doing well with public service accountability.¹³¹ The issues of state control and independence could have been addressed, but ‘legitimate perceptions of a conflict of interest’ arose due to the exchange regulator’s CEO being married to the CEO of Temasek

¹²³ Ian Austin, ‘Introduction Australia-Singapore Relations – Diplomatic, Strategic, Commercial and Cultural’ in Ian Patrick Austin (eds), *Australia-Singapore Relations: Successful Bilateral Relations in a Historical and Contemporary Context*, (Select Publishing, 2011) 1, 1.

¹²⁴ Ibid 3. Austin sees the political relationship as one of ‘strategic pragmatism...unencumbered by sentiment. If established elements of the relationship lose their relevance, they will invariably be dropped’.

¹²⁵ Ibid 11.

¹²⁶ Austin and Minaee, above n 101, 229.

¹²⁷ Foreign Investment Review Board, Australian Government, *Australia Welcomes Singapore Investors* <<http://www.firb.gov.au/content/singapore/welcome.asp> The Singapore desk listed on the FIRB website>.

¹²⁸ Austin, above n 123, 5.

¹²⁹ The Economist, ‘The Democracy Index 2011: Democracy Under Stress’ (White Paper, 2011) <http://www.eiu.com/public/topical_report.aspx?campaignid=DemocracyIndex2011>.

¹³⁰ World Economic Forum, *Singapore*, <<http://reports.weforum.org/global-competitiveness-report-2014-2015/economies/#indexId=GCI&economy=SGP>>, The World Economic Forum ranked Singapore second only to Switzerland in its *Global Competitiveness Report 2011-2012*.

¹³¹ The International Bank for Reconstruction and Development, ‘Doing Business 2011: Making a Difference for Entrepreneurs’ (Annual Report Series, World Bank, 1 June 2010) <<http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB11-FullReport.pdf>>.

Holdings.¹³² Not everyone is convinced that Temasek Holding is entirely transparent in its reporting.¹³³

Deidre Gerathy, general manager of FIRB's Foreign Investment and Trade Policy Division addressed issues associated with the 'nature of the investor'.¹³⁴ Murphy responded to questions as to why FIRB decided to 'go behind the corporates to see, in effect, who is the true owner of the entities'.¹³⁵ He said any level of direct, state-owned enterprise interest had to be declared during the application process, and implied that the case-by-case decision-making process, though laboriously individualised, was how this factor could best be taken into account.¹³⁶ The Committee discussion, abbreviated here, acknowledged the problem of SOE/GLCs but danced around whether it was decisive in this instance. At the end of the day, discretionary decision-making was in play.¹³⁷

Assuming that Temsaek Holding was a factor of concern for FIRB, their position was consistent with government policy that had developed in this area, specifically the principles that had emerged from the Senate the year before.¹³⁸ Treasurer Wayne Swan had announced the principles to assess foreign investment, focussed particularly on investment originating from state-owned enterprises and sovereign wealth funds. Principle 1 was relevant to the ASX-SGX proposed merger – it holds that the foreign investor should be at arm's length, embodying operational independence, from the foreign government. It goes on to say that 'whether the prospective investor's governance arrangements could facilitate actual or *potential control* by a foreign government' would also be taken into consideration.¹³⁹

¹³² Richard Ackland, 'A Loathsome Deal That Should be Given Bargepole Treatment', *The Sydney Morning Herald* (online), 29 October 2010 < <http://www.smh.com.au/federal-politics/political-opinion/a-loathsome-deal-that-should-be-given-bargepole-treatment-20101028-175lw.html> >.

¹³³ Christopher Balding, *Sovereign Wealth Funds: The New Intersection of Money and Politics* (Oxford University Press, 2012) 171. One academic conducting research on its accounts said that Temasek's stated returns 'do not appear to reflect the underlying asset-value returns'.

¹³⁴ Commonwealth, *Parliamentary Debates*, Senate, 1 June 2011, 82.

¹³⁵ Ibid 83.

¹³⁶ Ibid 84.

¹³⁷ Bath, above n 27, 13. A practice supported by case law, as Bath explains: 'The courts may review the procedural steps leading to the exercise of the discretion, and will consider the question of procedural fairness and natural justice and other administrative law grounds surrounding or leading up to a determination on the basis of national interest, but the national interest decision itself is one for the relevant minister'.

¹³⁸ Senate Economics References Committee, The Parliament of Australia, *Foreign Investment by State-owned Entities*, (2009).

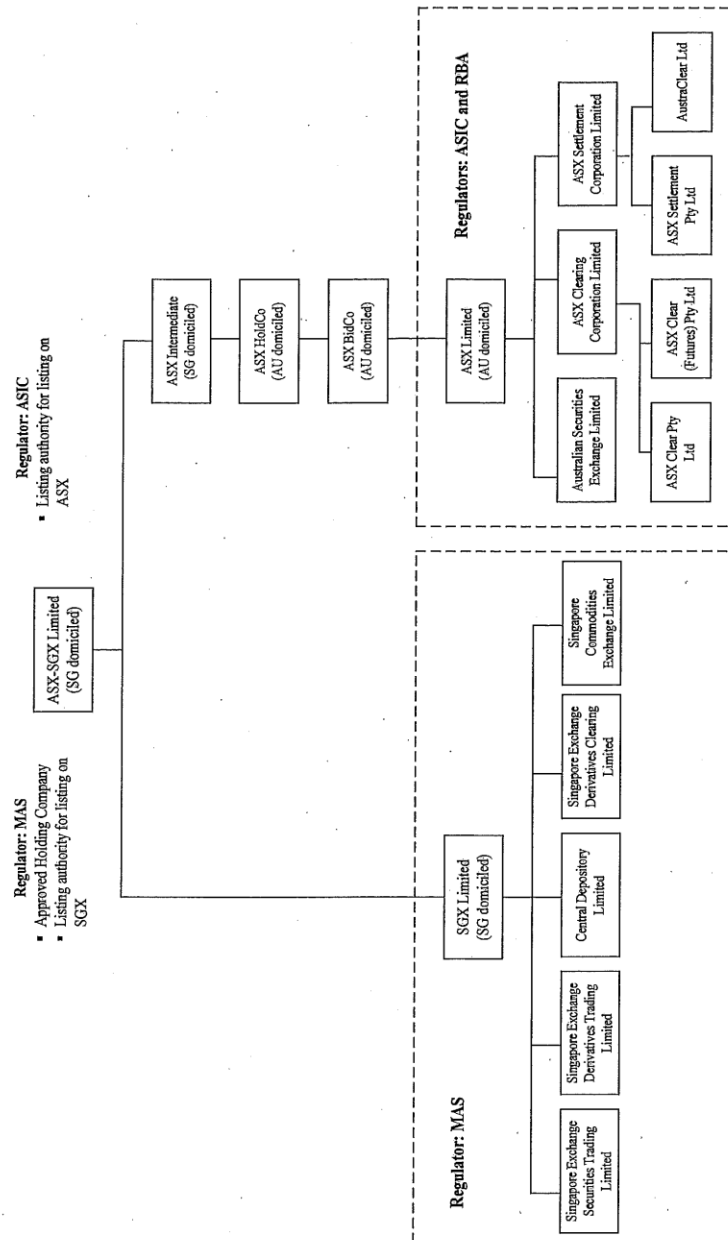
¹³⁹ Ibid Appendix 3. 'Treasurer's 2008 guidelines for assessing proposals by SOEs'.

Both of these issues would be relevant to the SGX bid. SGX could make a plausible case for operating independently of the Singapore government.¹⁴⁰ However, the element of ‘potential control’ would be harder for FIRB to dismiss given the proposed corporate group structure which would leave Temasek Holdings, a state-owned enterprise, with (at least) 23% ownership of the holding company ASX-SGX, domiciled in Singapore.

The FIRB minutes revealed the planned group structure, within which the new ASX-SGX entity would be a holding company (see Figure 1, below).

¹⁴⁰ Carlos D Ramirez and Ling Hui Tan, ‘Singapore, Inc. Versus the Private Sector: Are Government-linked Companies Different?’ (Working Papers, International Monetary Fund, July 2003). SOEs are typical of emerging economies. But their remnants are found throughout Asia, in the form of government-linked companies, or GLCs, which is the terminology used by the IMF and others. In 2003, the IMF found that Singapore’s GLCs are unusually competitive and do not seem to enjoy the privileged access to credit which often marks the GLC; but also found that they held an enhanced status in the market because of the association with government, which was quantified as a valuation premium of about 20%.

Figure



Although Singapore also follows the company law traditions of the common law system, as Australia does, it has long been recognised that the traditional independence of the incorporated entity, upheld by *Salomon v Salomon*,¹⁴¹ may be problematic in the presence of modern corporate group holdings. Because of the interconnectivity of a corporate group structure, and despite the regulatory firewalls that should be maintained, the commercial reality is that a holding company can, and often does, exert control over a subsidiary.¹⁴² In Australia, director's duties and other corporate law protocols are meant to deter group enterprise and prevent the profits of a subsidiary flowing upwards to the principal, in certain circumstances. Other abuses of the corporate group structure are not unknown – asset stripping, insolvency, insider dealing. The question was not whether Temasek or any other SOE would do that – it was that the change in ownership and the new group structure opened the door to the possibility – but the new entity would be domiciled in Singapore and beyond reach of Australian regulators. Control was being shifted, in more ways than one.

The minutes have been 'sanitised', that is, sensitive information has been removed. The text that remains from this process of selective disclosure leaves few clues to its former content.

VI CONCLUSION

Since the merger was blocked by the Treasurer, it is fruitless to consider whether Parliament would have passed a legislation allowing SGX to purchase 100% of the shares in ASX. But it is a cautionary tale and demonstrates how high the regulatory hurdles can be. The ASX's interest has been guarded heavily under Australian law, which requires a merger to be cleared by a number of authorities. A merger with the ASX not only has to be cleared by the Australian competition authority, it has to be scrutinised and approved by the FIRB, Treasurer and Parliament.

This failed attempt of the SGX provides a good illustration on the application of the national interest test in the financial securities sector. While the test may not require the deal to advance the national interest of Australia, it is necessary for the deal not to go against the

¹⁴¹ *Salomon v Salomon & Co* [1897] AC 22.

¹⁴² *Briggs v James Hardie & Co Pty Ltd* (1989) 16 NSWLR 549.

national interest. It is a question of fact on how the test is applied by the FIRB as the board will review application on a case by case basis. Despite the ambiguity of the threshold of the test, several indicia have proved to be decisive in the dismissal of the application of SGX. One of them is the integrated structure of ASX. In advising the Treasurer, the FIRB looked at the structure of control/practical control of the company, potential interference from foreign regulatory authorities; corporate structure, implication of the market and potential consequences of the merger in long run.

Part E The China Axis – Hong Kong, Shenzhen, Shanghai*

I INTRODUCTION

China's economy and capital markets have gone through unprecedented change over the last few decades. The return of Hong Kong to China in 1997 laid the foundation for closer cooperation between Hong Kong and mainland China. The clock is ticking and full political (and economic) integration is now barely 30 years away. Mainland China provides Hong Kong, previously a small but important market, with massive clout internationally; Hong Kong reciprocates by providing an international gateway to and from the mainland. Capital markets developments in Hong Kong and mainland China, and their stock exchanges in particular, presage the future. The question which inevitably arises: 'Will there be one China Stock Exchange?'

This chapter considers the structural organisation and regulatory framework of each of the three stock exchanges – Shanghai Stock Exchange (SSE), Shenzhen Stock Exchange (SZSE) and the Stock Exchange of Hong Kong (SEHK) – and the links and relationships among them. The ground-breaking Shanghai – Hong Kong Stock Connect, although off to a faltering start, is a sign of things to come. The big splash of Shanghai-Hong Kong Connect, however, has overshadowed other important structural initiatives vital to market development and integration: indices, product diversification and innovation, and back office operations.

II BACKGROUND: SSE, SZSE AND HKEX

A Stock Exchanges in Mainland China

1 Shanghai Stock Exchange (SSE)

Stock exchanges are not a brand new phenomenon in mainland China. The original Shanghai Stock Exchange dates back to 1891 when the Shanghai Sharebrokers Association, open to both domestic and international investors, began trading in stocks, debentures, government bonds and futures. The Sino-Japanese War halted operations in 1937. In 1946, operations resumed under the Shanghai Stock Exchange Co., Ltd. However, the Shanghai Stock Exchange Co., Ltd was short-lived, succumbing to the outcome of the Chinese revolution

three years later in 1949.¹

The modern Shanghai Stock Exchange (SSE) officially rose from the ashes some forty years later in November 1990. Operations began the following month. Modelled on the exchanges of the time in developed economies, the formal aspirations of the SSE were to provide a transparent, open, safe and efficient marketplace based on the stated principles of ‘legislation, supervision, self-regulation and standardization’. In the chaotic markets of ‘casino’ China, this was a tall order.

Unlike the New York Stock Exchange which is primarily an equity trading market, the SSE trades stocks, funds, bonds and derivatives, to the extent such products are permitted in China. Consistent with the formal compartmentalisation of Chinese company capital structure, the SSE Main Board only trades two types of shares: A-shares and B-shares. This bifurcation of capital structure, originally based on citizenship status of the holder of the shares, has been a defining characteristic of Chinese companies. A-shares are Renminbi (RMB) – dominated shares at their outset issued by Chinese domestic companies to domestic Chinese institutions, organisations and individuals. B-shares are a special category of ‘foreign’ share, denominated in RMB but trading in Shanghai in USD and in SZSE in HKD, and held by non-Chinese investors. This segregation of domestic and international investors in the domestic mainland Chinese markets produced unpleasant market and trading distortions and is slowly being eroded. For example, since 2001, mainland Chinese residents are allowed to invest in B-shares.² As of July 2015, there were 1062 A-shares and 53 B-shares listed on SSE, an indication of their relative significance.³

Funds or collective investment vehicles, a more recently permitted financial product, also trade on the SSE; there are 78 of them.⁴ The SSE also lists bonds, the most numerous of which are Unlisted Company Bonds (1624), followed by Listed Company Bonds (435), Treasury Bonds (263), Redeemable Bonds (21) and Convertible Bonds (5).⁵ The kinds of

* The author would like to acknowledge, in particular, the assistance of Dan Lu with this chapter.

¹ Shanghai Stock Exchange, *Historical Overview* (1 October 2015)
<<http://english.sse.com.cn/aboutsse/overview/historica/>>.

² «关于境内居民个人投资境内上市外资股若干问题的通知» [Notice on Issues Concerning Individual Domestic Residents' Investment in Foreign Currency Stocks Listed in the Domestic Stock Markets] (People's Republic of China) China Securities Regulatory Commission, Decree No 22, 22 February 2001.

³ Shanghai Stock Exchange, *Overview of Statistics (Stocks)* (27 July 2015)
<<http://www.sse.com.cn/assortment/stock/statistic/overview/>>.

⁴ Shanghai Stock Exchange, *Overview of Statistics (Funds)* (1 June 2015)
<<http://www.sse.com.cn/assortment/fund/closedendfund/general/>>.

⁵ Shanghai Stock Exchange, *Overview of Statistics (Bonds)* (1 June 2015)
<<http://www.sse.com.cn/assortment/bonds/statistic/general/>>.

bonds which can be created by mainland Chinese companies are quite restricted, limited essentially to simple instruments.

Trading in a limited array of derivative products has only been contemplated since January 2015 when the China Securities Regulatory Commission (CSRC) announced that SSE would carry out a stock option pilot program. Investors can now buy and sell options on 50ETF, an exchange-traded fund that tracks the 50 biggest RMB-dominated stocks on the SSE.⁶ Futures are traded in the China Financial Futures Exchange, which was jointly established by Shanghai Futures Exchange, Zhengzhou Commodity Exchange, Dalian Commodity Exchange, SSE and SZSE on 8 September 2006 in Shanghai.⁷ There are currently no warrants trading on the SSE.⁸

2 Shenzhen Stock Exchange (SZSE)

The city of Shenzhen shares a border with Hong Kong. The two cities are seamlessly linked by public transportation. It is easy to see the outlines of a future mega metropolis, with Hong Kong spilling without borders into Shenzhen. Such was not the case in December 1990 when the Shenzhen Stock Exchange (SZSE) was established, only a few weeks after the SSE. The SZSE is structured more like the London or Hong Kong exchanges, with their multiple listing boards designed for companies of different sizes and industry specialisation. SZSE has a Main Board, a SME Board and the ChiNext market (targeting the high tech industry).⁹ As of April 2015, SME Board listings dominated the market (746), with the Main Board trailing (468 A-share listings and 51 B-shares). The ChiNext market had 446 listings.¹⁰

Funds also trade on SZSE; there are 364 funds listed which include 41 ETFs.¹¹ Although the same kinds of bonds trade on both the SSE and the SZSE, the proportionate representation is very different. The SZSE market is dominated by Treasury Bonds (262) and Listed

⁶ China Securities Regulatory Commission, *CSRC Approves SSE Stock Option Pilot Program* (9 January 2015) <http://www.csrc.gov.cn/pub/newsite/zjhxwfb/xwdd/201501/t20150109_266372.html>.

⁷ China Financial Futures Exchange, *About CFFEX (Introduction)* (1 October 2015) <http://www.cffex.com.cn/en_new/gyjys_6434/jysjs/>.

⁸ Shanghai Stock Exchange, *Warrants (General)* (1 October 2015) <<http://www.sse.com.cn/assortment/warrants/statistics/general/>>.

⁹ The Main Board hosts the listings of large SOEs. The SME Board allows companies which cannot meet the requirements of the Main Board to be listed. The ChiNext is the first second board market targeting innovative and emerging industries such as hi-tech industries.

¹⁰ Shenzhen Stock Exchange, *Overview of Listed Securities* (30 April 2015) <<http://www.szse.cn/main/files/2015/05/07/RM020102.html>>.

¹¹ Shenzhen Stock Exchange, *Market Data (Fund List)* (28 July 2015) <<http://www.szse.cn/main/marketdata/jypz/fundlist1/>>.

Company Bonds (211). Only a negligible number of Unlisted Company Bonds (30), Redeemable Bonds (9) and Convertible Bonds (7) are traded there.¹²

Since 2000, the SZSE has taken a very outward looking stance, signing Memoranda of Understandings (MOUs) with 30 major stock exchanges and financial institutions around the world in the interests of enhancing cross-border cooperation and communications. SZSE has also taken an active part in international securities organisations. SZSE is a member of both the World Federation of Exchanges (WFE) and the Asian and Oceanian Stock Exchanges Federation (AOSEF). It is also an affiliate member of the International Organization of Securities Commissions (IOSCO).¹³

3 Regulatory Framework in Mainland China

Having been established prior to the waves of demutualisation that swept through exchanges around the world, the SSE and SZSE emulate a now old-fashioned model (think NYSE, prior to 2007), the nominally self-regulatory mutual associations based on a membership structure.¹⁴ Only Chinese domestic securities institutions with legal entity status can apply to become a member of the stock exchange.¹⁵ Securities institutions must obtain membership in order to participate in centralised trading which is a call auction system.¹⁶

Both SSE and SZSE are subject to the supervision and control of the centralised CSRC in Beijing.¹⁷ Control is the operative word. Both exchanges, in fact, predate the CSRC, as they were originally constituted and operated under local administrative rules in the special economic zones of Shanghai and Shenzhen. The exchanges in 1990 were an experiment, a tentative toe dipping into the unknown seas of capitalism. ‘Let’s try it and see what happens’,¹⁸ then leader Deng Xiaoping famously said. Exchange operations are now closely monitored and controlled by the CSRC. The exchanges perform the traditional functions of exchanges around the world: providing the venue and facilities for securities trading; formulating operational rules; receiving listing applications and arranging securities listing;

¹² Shenzhen Stock Exchange, *Market Data (Bond)* (28 July 2015) <<http://www.szse.cn/main/marketdata/jypz/zqlb/>>.

¹³ Shenzhen Stock Exchange, *Overview* (28 July 2015) <<http://www.szse.cn/main/en/AboutSZSE/SZSEOverview/>>.

¹⁴ «证券交易所管理办法» [Measures for the Administration of Securities Exchanges] (People's Republic of China), China Securities Regulatory Commission, Decree No 4, 12 December 2001, art 3.

¹⁵ Ibid art 41.

¹⁶ «中华人民共和国证券法 (2014 年修正)» [Securities Law of the People's Republic of China (2014 Amendment)] (People's Republic of China), Standing Committee of the National People's Congress, Order No. 14 of the President of the People's Republic of China, 31 August 2014, art 103.

¹⁷ «证券交易所管理办法», above n 14, art 4.

¹⁸ 黄金平, 张励 [Jinping Huang, Li Zhang] «邓小平改革开放初期在上海» [Deng Xiaoping in Shanghai During the Early Days of the Open Door Policy] (5 September 2014) 中国共产党历史网 [Communist Party of China History Website] <<http://www.zgdsw.org.cn/n/2014/0905/c375621-25612583.html>>.

organising and supervising securities trading, supervising members; regulating listed companies; managing and disseminating market information and other functions, all under the watchful gaze of the CSRC and subject to its approval and intervention.¹⁹

The SSE and SZSE exercise the three primary functions of traditional exchanges: regulation of listed companies, monitoring of market transactions and supervision of members. In Shanghai, these three functions are carried out by the Listed Company Supervision Department I and II, the Market Surveillance Department and the Membership Department.²⁰ In Shenzhen, the internal organisation is somewhat different, the Main Board/SME Board/ChiNext Market Compliance and Disclosure Departments, Market Surveillance Department and Membership Supervision Department.²¹

4 Internal Governance of Mainland China Stock Exchanges

Reflecting the mutual association model, stock exchanges in China have two decision making bodies, the Members' Meeting and the Board of Directors, as well as specialised committees.²² The Members' Meeting (known as the General Assembly in Shanghai and the Members' Assembly in Shenzhen) is the ultimate decision-maker in this structure, at least in theory.²³ Powers of the Members' Meeting are typical of mutual associations: formulation and revision of the articles of association of the stock exchange (subject to the final approval of CSRC); election and dismissal of member appointees to the Board of Directors; review and adoption of the reports of the Board of Directors and the general manager; review and adoption of the financial budget and financial statements, or "final settlement report", and decisions on other major matters of the exchange.²⁴ The Board of Directors must convene a Members' Meeting once a year.²⁵ Ad hoc Members' Meetings can be convened if the number of directors falls below the minimum required by law,²⁶ or at the request of over one third of all members,²⁷ or when the Board of Directors deems it necessary.²⁸

¹⁹ «证券交易所管理办法», above n 14, art 11.

²⁰ Shanghai Stock Exchange, *Organizational Structure* (28 July 2015) <<http://english.sse.com.cn/aboutsse/sseoverview/organizational/>>.

²¹ Ibid.

²² «证券交易所管理办法», above n 14, art 16.

²³ Ibid art 17.

²⁴ Ibid.

²⁵ Ibid art 18.

²⁶ Ibid.

²⁷ Ibid art 18(2).

²⁸ Ibid art 18(3).

The Board of Directors, the other decision-making body of the stock exchange,²⁹ is known as the Board of Governors in SSE and the Board of Directors in SZSE.³⁰ Again, very traditional powers are allocated to the Board of Directors: implementing the resolutions of the Members' Meeting,³¹ formulating and revising the rules of the stock exchange,³² reviewing and approving the business plan proposed by the general manager,³³ reviewing and approving the budgets and financial statements submitted by the general manager,³⁴ reviewing and approving membership applications,³⁵ reviewing and approving disciplinary action against members,³⁶ establishing specialised committees when necessary³⁷ and other responsibilities as authorised by the Members' Meeting.³⁸

The Board of Directors consists of seven to 13 directors, including member directors and non-member directors. Here is where exchange governance differs from traditional mutual association exchanges. Member directors are elected by the Members' Meeting whereas the non-member directors are appointed by the regulator, the CSRC.³⁹ The number of non-member directors can vary between one third and one half of the total number of directors.⁴⁰ To avoid entrenchment, a director can serve no more than two consecutive terms.⁴¹ The Board of Directors has one chairman and one or two vice chairmen, nominated by the CSRC and elected by the Board of Directors.⁴² The Chairman is responsible for convening and chairing the Board of Directors' meeting and serves as a chair for Members' Meeting.⁴³

The Board of Directors must meet at least once every quarter; there is a high quorum requirement of two thirds of the members of the Board.⁴⁴ Again, a high threshold, or supermajority of two thirds of the directors present at the meeting is required to pass resolutions.⁴⁵ These, greater than a simple majority provisions, act to give the CSRC a veto

²⁹ «中华人民共和国证券法 (2014 年修正)», above n 16, art 20.

³⁰ Shanghai Stock Exchange, *Organizational Structure*, above n 20; Shenzhen Stock Exchange, *Organization Structure* (28 July 2015) <<http://www.szse.cn/main/en/aboutszse/organizationstructure/>>.

³¹ «中华人民共和国证券法(2014 年修正)», above n 16, art 20(1).

³² Ibid art 20(2).

³³ Ibid art 20(3).

³⁴ Ibid art 20(4).

³⁵ Ibid art 20(5).

³⁶ Ibid art 20(6).

³⁷ Ibid art 20(7).

³⁸ Ibid art 20(8).

³⁹ «证券交易所管理办法», above n 14, art 21.

⁴⁰ Ibid.

⁴¹ Ibid.

⁴² Ibid art 22.

⁴³ Ibid art 23.

⁴⁴ Ibid art 21.

⁴⁵ Ibid.

on exchange activities. Resolutions passed by the Board of Directors must be filed with the CSRC.⁴⁶

In addition to the Members' Meeting and the Board of Directors, the stock exchange is required to have a general manager and one to three deputy general managers. The position of 'General Manager' is known as the 'President Office' in SSE and SZSE. Both general manager and deputy general managers are appointed by the CSRC. These positions cannot be held by state public servants concurrently with their service in that capacity.⁴⁷ The general manager serves a three year term, for no more than two consecutive terms.⁴⁸ Under the direction of the Board of Directors, the general manager is the legal representative of the exchange, responsible for its day to day management.⁴⁹ The general manager is a member, but cannot be chairman, of the Board of Directors.⁵⁰

Echoing the dual board structure of German-inspired Chinese companies law, a stock exchange must also have a supervisory committee, the members of which serve a three year term.⁵¹ The chairman of the Board of Directors serves concurrently as the chairman of the supervisory committee.⁵² The supervisory committee is accountable to the Board of Directors.⁵³ In the SSE, this function takes the form of 'Board of Supervisors', effectively a dual board structure.⁵⁴ The SZSE, on the other hand, has no supervisory committee in its organisational chart,⁵⁵ but the SZSE Articles of Association do provide for the establishment of a supervisory board for the purpose of monitoring its business and financial operations.⁵⁶ The supervisory committee is designated to oversee high-level management personnel and other staff members of the stock exchange, especially in their compliance with laws and regulations and execution of the resolutions adopted by the Members' Meeting and the Board of Directors.⁵⁷ The supervisory committee also monitors the financial position of the exchange.⁵⁸

⁴⁶ Ibid.

⁴⁷ Ibid art 24.

⁴⁸ Ibid.

⁴⁹ Ibid.

⁵⁰ Ibid art 22.

⁵¹ Ibid art 26.

⁵² Ibid.

⁵³ Ibid.

⁵⁴ Shanghai Stock Exchange, *Organizational Structure*, above n 20.

⁵⁵ Ibid.

⁵⁶ Articles of Association for Shenzhen Stock Exchange, adopted at the 2nd General Members Meeting on 20 May 1993, art 27.

⁵⁷ «证券交易所管理办法», above n 14, art 26.

⁵⁸ Ibid.

5 Weaknesses in Internal Governance

In China, the self-regulatory function of stock exchanges is a mere legal formality, a vestige of the traditional Anglo-American exchange model. The exchanges are tightly controlled by the Chinese government. For example, stock exchanges have no power to appoint middle and top management. They are obliged to register the appointment of senior management staff with the CRSC. Approval of the CSRC is required for appointment of Finance Manager and Human Resources Manager.⁵⁹ Core functions such as formulating listing rules and reviewing listing applications are exercised by the CSRC, not the exchanges.⁶⁰

B Hong Kong Exchanges and Clearing Limited (HKEx)

1 Functions and Products

The Hong Kong Exchange and Clearing Limited (HKEx) is both an exchange and clearing house operator. In 1999, the Stock Exchange of Hong Kong and the Hong Kong Futures Exchange Limited were demutualised and grouped together with Hong Kong Securities Clearing Company Limited under the single holding company, HKEx.⁶¹

Thus HKEx operates the only stock and future market in Hong Kong through its wholly owned subsidiaries, the Stock Exchange of Hong Kong Limited (SEHK) and the Hong Kong Futures Exchange Limited (HKFE). HKEx also operates four clearing houses through its subsidiaries, Hong Kong Securities Clearing Company Limited (HKSCC), HKFE Clearing Corporation Limited (HKCC), SEHK Options Clearing House Limited (SEOCH) and OTC Clearing Hong Kong Limited (OTC Clear). HKSCC, HKCC and SEOCH provide integrated clearing, settlement, depository and nominee services to their participants, while OTC Clear provides OTC interest rate derivatives and non-deliverable forwards clearing and settlement services.⁶² In addition to its Hong Kong subsidiaries, HKEx took over the London Metal Exchange (LME) in 2012. According to its 2013-2015 Mission Statement, HKEx aims to be ‘the global exchange of choice for our China clients and our international clients seeking China exposure’.⁶³

⁵⁹ Ibid art 25.

⁶⁰ Jin Qiang, *The Research of the Demutualization of the Global Stock Exchanges and the Improvement of the Securities Market's Governance of China* (PhD Thesis, Nankai University, 2013), 131.

⁶¹ Hong Kong Exchanges and Clearing Limited, *History of HKEx and its Markets* (31 October 2013) <<http://www.HKEx.com.hk/eng/exchange/corpinfo/history/history.htm>>.

⁶² Ibid.

⁶³ Hong Kong Exchanges and Clearing Limited, *Company Profile* (31 October 2013) <<http://www.HKEx.com.hk/eng/exchange/corpinfo/profile.htm>>.

HKEx also exercises certain self-regulatory authority over listed companies in Hong Kong. It is responsible for administering the listing, trading and clearing rules on its exchanges. Like London, the SEHK has multitiered trading facilities: the Main Board for large capitalisation companies and the Growth Enterprise Market (GEM), the name of which is self-explanatory. Until recently at least, the SEHK has been the trading venue of choice for the shares of mainland Chinese companies (especially state-owned enterprises) wishing to attract international investors. The shares of these mainland Chinese companies listed on the SEHK are referred to, appropriately enough, as ‘H-shares’.

HKEx offers trading in the full gamut of both securities and derivatives products. Securities products include equity securities, depository receipts, so-called “stapled” securities (different securities of the same issuer listed and traded as a bundle at one single price), debt securities, ETFs, REITs, derivative warrants, callable bull/bear contracts, and listed equity linked instruments (some of which may in fact meet the usual definition of a derivative).⁶⁴ Derivatives products reflect the older products historically traded on a separate exchange, equity index products, stock futures and options, RMB currency futures, as well as HIBOR futures and commodities products.⁶⁵ Not surprisingly, the Hong Kong markets display much greater diversity and a more sophisticated range of financial products when compared to mainland China.

2 Regulatory Framework

In the older British tradition, the SEHK exercised self-regulatory powers, primarily with respect to the listing process and the supervision of listed companies. It has a statutory duty to ensure, as far as reasonably practicable, that the Hong Kong markets are fair, orderly and informed. However, the Securities and Futures Commission (SFC), a regulator created in 1989 in the aftermath of embarrassing market failures in Hong Kong, has been steadily encroaching on the traditional preserve of exchange self-regulation. In 2001, the responsibility for regulating prudential aspects of the market and the conduct of market players was shifted from SEHK to the SFC, ending protracted turf wars between the two. This shift exemplifies yet again how crisis, in this case the Asian Financial Crisis of 1997-98,

⁶⁴ Hong Kong Exchanges and Clearing Limited, *Securities Products* (28 July 2015) <<https://www.HKEx.com.hk/eng/prod/secprod/CMProducts.htm>>.

⁶⁵ Ibid.

provokes change in long disputed regulatory boundaries.⁶⁶ Since 2001, the Hong Kong SFC has taken the lead in market regulation and certain aspects of the listing process, its assertion of authority buttressed by similar developments in London. The SFC supervises and monitors the SEHK's performance of its listing-related functions and responsibilities. Under the dual filing regime, SEHK passes on disclosure materials submitted by listing applicants to SFC and SFC can object to a listing if it considers the disclosure material to be false or misleading.⁶⁷ While SEHK is responsible for formulating and amending the Listing Rules, SFC approval is required for amendments and policies if the new rules are mandatory or generally applicable.⁶⁸

3 Internal Governance

HKEx is not only the sole operator of exchange-based stock and futures markets in Hong Kong but also a listed company in its own right. This mixture of public function and profit making purpose as a listed company has given rise to a more stringent internal governance framework than evidenced in its mainland counterparts which are more directly controlled by the regulator.

The Board of Directors is responsible for managing the business of HKEx and its subsidiaries, directly and indirectly through its committees. The Board of Directors provides the leadership and oversight to management in terms of promoting actions consistent with the public interest as well as its shareholders. Public interests prevail in case of conflict.⁶⁹ The Board of Directors is also responsible for establishing corporate policies, formulating strategic plans, implementing and maintaining effective internal controls and overseeing management practices.⁷⁰ The Board of Directors consists of two to 13 members. Shareholders can elect up to six directors and the Financial Secretary of the Hong Kong Special Administrative Region Government can appoint a maximum of six directors.⁷¹ Consistent with modern notions of corporate governance, the Chairman of the Board of Directors must be a non-executive director but additionally, reflecting the interaction of politics and the

⁶⁶ Memorandum of Understanding Between Securities and Futures Commission and Hong Kong Exchanges and Clearing Limited on Matters Relating to SFC Oversight, Supervision of Exchange Participants and Market Surveillance signed 25 February 2001, art 2.5.

⁶⁷ Ibid art 14.

⁶⁸ Hong Kong Exchanges and Clearing Limited, *Introduction to Regulatory Framework* (31 October 2013) <<https://www.HKEx.com.hk/eng/rulesreg/regintro/introreg.htm>>.

⁶⁹ Hong Kong Exchanges and Clearing Limited, *Terms of Reference and Modus Operandi of the Board of Hong Kong Exchanges and Clearing Ltd* (July 2014), art 11.

⁷⁰ Ibid.

⁷¹ Ibid art 1.

market in Hong Kong, his or her appointment is subject to the approval of the Chief Executive of the Hong Kong SAR.⁷²

The Board of Directors can delegate any of its powers and functions to appropriate committees and panels formed for such purpose.⁷³ Again exemplifying current thinking in best practices for corporate governance, there are nine board committees: Audit Committee, Environmental, Social and Governance Committee, Executive Committee, Investment Advisory Committee, Nomination Committee, Panel Member Nomination Committee, Remuneration Committee, Risk Committee and Risk Management Committee.⁷⁴ Each committee is chaired by an independent non-executive director (INED) and comprises a majority of INEDs, except for the Risk Management Committee whose composition is stipulated in section 65 of the Securities and Futures Ordinance. The committees hold meetings regularly and follow the procedures for Board of Directors meetings. They are authorised to seek independent advice from external advisers if necessary at the expense of HKEx. The company secretary assists the Chairman in advancing the highest standards of corporate governance and the effective operation of the board and its committees.⁷⁵

The Management Committee is the most powerful decision making body, headed by the chief executive. Its main responsibilities include monitoring operation of the company, making recommendations to the Board of Directors and the executive committee, approving operational and capital expenditures, ensuring compliance with statutory obligations by the company and supervising its relationship with all regulatory authorities.⁷⁶

In addition, there are three Consultative Panels – Cash Market Consultative Panel, Derivatives Consultative Panel and Clearing Consultative Panel – which are designed to provide market expertise and advice to the Board of Directors on issues such as international market trends, technological developments, the needs of market participants and potential product opportunities relating to HKEx.⁷⁷

III FORMAL AGREEMENTS AND COOPERATION

⁷² Ibid art 4.

⁷³ Ibid art 11(d)(v).

⁷⁴ Hong Kong Exchanges and Clearing Limited, *Committees and Consultative Panels* (1 June 2015) <<http://www.HKEx.com.hk/eng/exchange/org/commember.htm>>.

⁷⁵ Hong Kong Exchanges and Clearing Limited, *Articles of Association of Hong Kong Exchanges and Limited* (April 2014), art 115-117.

⁷⁶ Hong Kong Exchanges and Clearing Limited, *Management Committee* (19 June 2015) <<http://www.HKEx.com.hk/eng/exchange/org/mgtcom/mgtcom.htm>>.

⁷⁷ Hong Kong Exchanges and Clearing Limited, *Committees and Consultative Panels*, above n 74.

A Agreements for mutual exchange of securities market and listed company data (2001)

In 2001, HKEx, SZSE and SSE entered into agreements on the exchange and publication of securities market and listed company data from the three securities exchanges. These agreements aimed to provide investors with direct and convenient access to data and to promote cooperation and information sharing among the three stock exchanges.⁷⁸

B Market Data Collaboration Agreements (2009)

In modern markets, information has become a lucrative commodity; exchanges are well-positioned to collect it and have embarked on commercial ventures to sell it. Since 2009, the wholly-owned information business subsidiaries of HKEx and Shanghai Stock Exchange (SSE) have established a market data collaboration programme.⁷⁹ Under the programme, both parties are entitled to redistribute the other party's basic real-time market data of companies listed on both SEHK and SSE to their own authorised information vendors (IVs) for onward transmission to the IVs' subscribers for internal display purposes. A similar market data collaboration programme was also entered into between SEHK and SZSE a year later in 2010.⁸⁰

C Shanghai – Hong Kong and Shenzhen – Hong Kong Closer Cooperation Agreement (2009)

In 2009, HKEx entered into a Closer Cooperation Agreement with both SSE and SZSE to strengthen their cooperation on information sharing, product development and personnel training.⁸¹ Given the increase in A-share and H-share listings, HKEx and SSE engage in a regular exchange of opinions on operational issues in regulating the securities market and information disclosure.⁸² There were also joint initiatives in product development such as cross-border ETFs linked to H-shares or A-shares.

D Shanghai – Hong Kong Stock Connect

⁷⁸ 'HKEx Reaches Agreement with Shanghai Stock Exchange and Shenzhen Stock Exchange to Exchange Securities Market Data', *Mondo Visione* (online), 31 May 2001 <<http://www.mondovisione.com/media-and-resources/news/HKEx-reaches-agreement-with-shanghai-stock-exchange-and-shenzhen-stock-exchange/>>.

⁷⁹ Hong Kong Exchanges and Clearing Limited, *HKEx and SSE Sign Market Data Collaboration Agreement* (October 2008) <<http://www.HKEx.com.hk/eng/newsconsul/newsltr/2008/documents/2008-10-06-e.pdf>>.

⁸⁰ Hong Kong Exchanges and Clearing Limited, *HKEx and SZSE Subsidiaries Sign Market Data Collaboration Agreement* (14 April 2010) <<http://www.hkgem.com/eng/newsconsul/HKExnews/2010/100414news.htm>>.

⁸¹ Hong Kong Exchanges and Clearing Limited and Shanghai Stock Exchange, *Joint Statement on Closer Cooperation Between the Shanghai Stock Exchange and Hong Kong Exchanges and Clearing* (21 January 2010) M2 <<http://www.m2.com/m2/web/story.php/2010618D6A48FC9A48F0802576B30027C62C>>.

⁸² 'Joint Statement on Closer Cooperation between the Shanghai Stock Exchange and Hong Kong Exchanges and Clearing', *Mondo Visione* (online), 21 January 2010 <<http://www.mondovisione.com/media-and-resources/news/joint-statement-on-closer-cooperation-between-the-shanghai-stock-exchange-and-ho/>>.

1 Rationale and Significance

During China's Third Plenum of the 18th Party Congress in November 2013, financial market reform, such as increasing mutual access between domestic and international capital markets, was emphasised as the key component of China's overall comprehensive and deepened reform.⁸³ The Shanghai – Hong Kong Stock Connect was an initiative launched by Premier Li Keqiang as an important step toward the opening up of Chinese capital market to international investment. Shanghai-Hong Kong Stock Connect is thus as much a high level political gesture, as a market enhancing initiative.

The programme provides an alternative channel for international investors to access China's securities markets, adding to the existing schemes for Qualified Foreign Institutional Investors (QFII) and Renminbi Qualified Foreign Institutional Investors (RQFII) which developed over the last decade or so. The Shanghai – Hong Kong Stock Connect, for the first time, permits international retail, as opposed to institutional, investors to trade Chinese shares. The Shanghai – Hong Kong Stock Connect is also of regulatory significance as it lays the groundwork for further bilateral regulatory cooperation between the CSRC and SFC. The bilateral MOU envisages a closer relationship between the two regulators on market surveillance, enforcement and information sharing in their common effort to enhance market integrity.⁸⁴

2 The Mechanism

In the usual incremental Chinese fashion, the Shanghai – Hong Kong Stock Connect is a pilot programme set up between the SSE, the SEHK, China Securities and Clearing Corporation Limited (ChinaClear) and Hong Kong Securities Company Limited (HKSCC). The programme is designed to establish mutual access between stock markets in mainland China and Hong Kong. Investors in Mainland China and Hong Kong can place orders and trade eligible shares listed on the participating stock exchanges through their local securities brokers.⁸⁵

⁸³ *Decision of the Central Committee of the Communist Party of China on Some Major Issues Concerning Comprehensively Deepening the Reform* (People's Republic of China) Adopted at the Third Plenary Session of the 18th Central Committee of Communist Party of China on 12 November 2013.

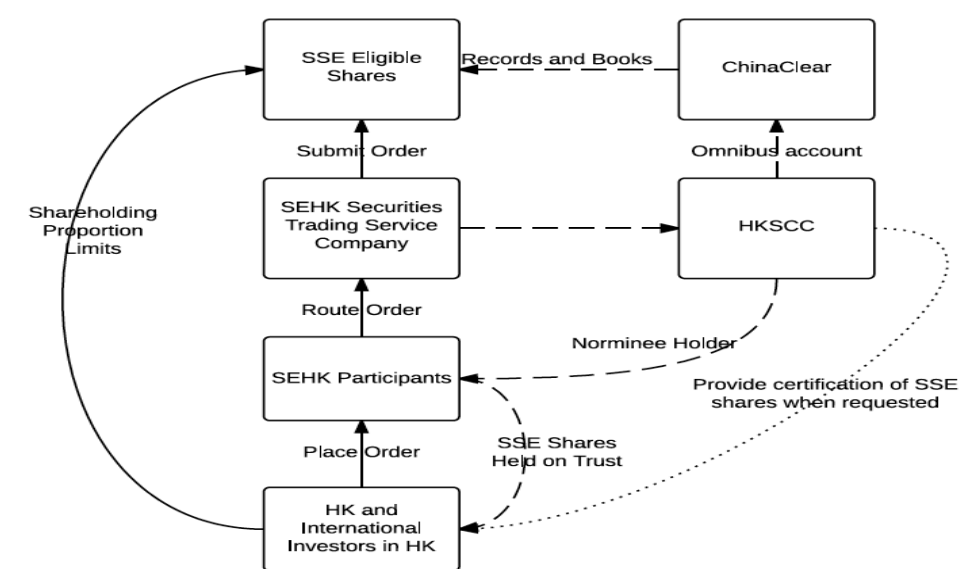
⁸⁴ China Securities Regulatory Commission and Securities and Futures Commission, *Memorandum of Understanding between the CSRC and the SFC on Strengthening of Regulatory and Enforcement Cooperation under Shanghai-Hong Kong Stock Connect*, 17 October 2014 <http://www.sfc.hk/web/files/ER/MOU/ENF_MOU_October2014.pdf>.

⁸⁵ Hong Kong Securities and Futures Commission, 'Joint Announcement of China Securities Regulatory Commission and Securities and Futures Commission' (News Release, 10 April 2014) <<https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=14PR41>>.

The programme consists of a Northbound Trading Link through which Hong Kong and international investors purchase SSE listed shares through Hong Kong brokers, and a Southbound Trading Link through which mainland China investors buy SEHK listed shares through mainland China securities firms.⁸⁶ Investors place orders through their local brokers and the local brokers then channel the orders to the other exchange through their local exchange.

Daily quota and aggregate total of shares traded are imposed on both the Southbound and Northbound Trading Link. HKEx CEO Charles Li indicated that the quota may be eliminated in future.⁸⁷

3 Northbound Trading Link



The Northbound Trading Link is subject to an aggregate quota of RMB300 billion and a daily quota of RMB13 billion.⁸⁸ SEHK Securities Trading Service Company is responsible for monitoring the quotas.⁸⁹ SEHK Securities Trading Service Company applies to become a ‘SSE Participant’ (although not a member) and obtain status as a ‘Principle Business Unit’.⁹⁰ Principle Business Unit status gives the SSE Participant the right to carry out transactions on

⁸⁶ Ibid I.

⁸⁷ «李小加：沪港通的额度最终可以取消» [Charles Li: Quota for Shanghai-Hong Kong Stock Connect Could be Eliminated in Future] (22 May 2015) 腾讯财经 [Tencent Finance] <<http://finance.qq.com/a/20140522/026327.htm>>.

⁸⁸ Hong Kong Securities and Futures Commission, above n 85, III(d).

⁸⁹ Shanghai Stock Exchange, *Measures for Shanghai – Hong Kong Stock Connect Pilot Program by the Shanghai Stock Exchange* (2014), art 38 <<http://english.sse.com.cn/investors/shhkconnect/rules/regulatory/a/20150213/05a11b6e019f062ac8320d4af376effc.pdf>> (*‘Measures for Pilot Program’*).

⁹⁰ Ibid art 4.

the trading facility of SSE but also subjects the SSE Participant to the regulation of SSE with respect to the relevant securities. Principle Business Unit status is the basis on which SSE Participant's transactions and trading authority are managed by the SSE.]

There are 568 SSE listed shares eligible for trading under the Northbound Trading Link, including all the constituents of the SSE 180 Index and SSE 380 Index, and shares of all SSE-listed companies which have issued both A-shares and H-shares.⁹¹ An individual investor cannot hold more than 10% of the total shares of a SSE-listed company.⁹²

Hong Kong investors and international investors in Hong Kong place orders for Shanghai Stock Connect shares with SEHK Participants (i.e. local Hong Kong brokers) who then route orders to the SEHK Securities Trading Service Company.⁹³ SEHK Securities Trading Service Company submits orders to the SSE. All Shanghai Stock Connect shares are quoted and traded in RMB.⁹⁴ Before accepting a client's "sell" order, SEHK Participants (a broker-dealer admitted and registered to trade on SEHK) must ensure there are sufficient securities available in the client's account.⁹⁵ Shanghai Stock Connect shares cannot be sold before delivery.⁹⁶

The HKSCC is responsible for the clearing and settlement of all Shanghai Stock Connect shares.⁹⁷ The Several Provisions on the Pilot Program of Shanghai-Hong Kong Stock Market Connect promulgated by the CSRC expressly provides that all Shanghai Stock Connect shares are registered in the name of HKSCC in the Securities Depository and Clearing Company Limited (ChinaClear)'s books as the nominee holder for HKSCC Participants and the underlying investors.⁹⁸ All Shanghai Stock Connect shares are held in an omnibus stock account in the name of HKSCC and this account is separate from accounts of other clearing participants of ChinaClear. In case of the insolvency of ChinaClear, shares held under HKSCC's omnibus stock account will not form part of ChinaClear's assets and will not be

⁹¹ Ibid art 16.

⁹² «沪港股票市场交易互联互通机制试点若干规定» [Provisions on the Shanghai-Hong Kong Stock Connect Pilot Program] (People's Republic of China) Chinese Securities Regulatory Commission, Order No 101 (13 June 2014), art 12 ('CSRC Provisions').

⁹³ Ibid art 6.

⁹⁴ Shanghai Stock Exchange, *Measures for Pilot Program*, above n 89, art 20.

⁹⁵ Ibid art 30.

⁹⁶ Ibid art 31.

⁹⁷ Hong Kong Exchanges and Clearing Limited, *Issues Concerning Shanghai-Hong Kong Stock Connect* (December 2014) <<https://www.hkex.com.hk/eng/newsconsul/hkexnews/2015/Documents/Issues%20concerning%20Shanghai-Hong%20Kong%20Stock%20Connect.pdf>>.

⁹⁸ CSRC Provisions, above n 92, art 7(4).

available for distribution to ChinaClear's creditors. Securities registration records issued by ChinaClear evidence HKSCC's holding of Shanghai Stock Connect shares.⁹⁹

At the HKSCC level, "Participants (ie SEHK Participants who have entered into arrangements with HKSCC for securities clearing) holding in Shanghai Stock Connect shares are recorded in their respective stock accounts in the Central Clearing and Settlement System (CCASS) of HKSCC. HKSCC Participants can hold clients' securities in CCASS on an omnibus basis or through individual stock segregated accounts."¹⁰⁰

At HKSCC Participant's level, the Shanghai Stock Connect shares are held for clients in the books and records of HKSCC Participants. Under Hong Kong law, securities held by intermediaries are held on trust on a fiduciary basis and do not form part of the intermediaries' assets.¹⁰¹

Even though the beneficial ownership in the SSE shares of Hong Kong and international investors is recognised under mainland China law, there is no legal mechanism or guidance for ascertaining and confirming the identity of the beneficial owners in the SSE shares held by HKSCC.¹⁰² In order to address this commonly raised concern from international mutual fund investors, the HK central clearing authority, CCASS, amended its settlement rules to provide further assurance. The new rule stipulates that in the event that a beneficial owner of SSE shares decides to bring a legal proceeding in mainland China to enforce its rights relating to SSE shares, the HKSCC will provide certification as an evidential proof to verify beneficial ownership. HKSCC may also assist in bringing legal action in mainland China if necessary.¹⁰³

4 Southbound Trading Link

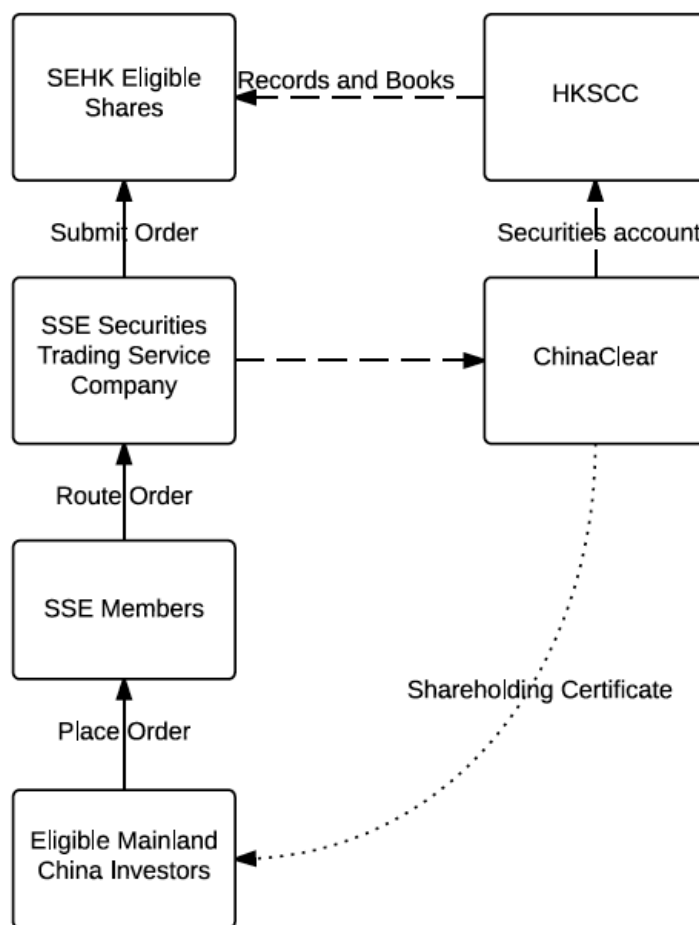
⁹⁹ Hong Kong Exchanges and Clearing Limited, *Issues Concerning Shanghai-Hong Kong Stock Connect*, above n 97.

¹⁰⁰ Ibid No 10.

¹⁰¹ Ibid No 11.

¹⁰² Aly Song, 'The Through Train: Stock Connect's Impact and Future' (Report, ASIFMA & Thomson Reuters, December 2014) 10 < <http://share.thomsonreuters.com/assets/forms/shanghai-hk-stock-connect-1008885.pdf> >.

¹⁰³ Hong Kong Exchanges and Clearing Limited, *General Rules of Central Clearing and Settlement System* (30 March 2015), r 824 < <https://www.hkex.com.hk/eng/rulesreg/clearrules/ccassgr/ccassrule.htm> > ('General Rules of CCASS').



The Southbound Trading Link is subject to an aggregate quota of RMB250 billion and a daily quota of RMB10.5 billion.¹⁰⁴ There are 268 shares eligible for the Southbound Trading Link: all the constituents of the Hang Seng Composite LargeCap Index, the Hang Seng Composite MidCap Index and shares of all companies crosslisted on the SSE and SEHK.¹⁰⁵ All Hong Kong Stock Connect shares are quoted in HKD but settled in RMB.¹⁰⁶ In addition, only those institutional investors or individual investors who hold an aggregate balance of no less than RMB 500,000 in their securities and cash accounts are eligible to participate in the Southbound Trading Link.¹⁰⁷ No minimum asset requirement is imposed on northbound investors.

Mainland China investors place their orders with SSE members (mainland China securities firms) which route these orders to SSE Securities Trading Service Company. The SSE

¹⁰⁴ Hong Kong Securities and Futures Commission, above n 85, III(d).

¹⁰⁵ Shanghai Stock Exchange, *Measures for Pilot Program*, above n 89, art 57.

¹⁰⁶ Ibid art 62.

¹⁰⁷ Ibid art 86.

Securities Trading Service Company then submits such orders to SEHK.¹⁰⁸ SSE members must ensure there are sufficient funds or securities in their clients' accounts before accepting orders.¹⁰⁹ Hong Kong Stock Connect shares can be sold before settlement on the same trading day once the transaction is confirmed.¹¹⁰ SEHK adopts T+2 in securities settlement thus investors obtain proprietary interests two days after settlement.¹¹¹

Similarly to the Northbound Trading Link, Hong Kong Stock Connect shares bought by mainland investors are recorded in a securities account held by ChinaClear with HKSCC.¹¹² The shareholding certificate issued by ChinaClear serves as valid evidence of investors' legal entitlement to their Hong Kong Stock Connect shares. No paper share certificate is provided.¹¹³ ChinaClear is required to consult investors prior to exercising any rights associated with the shares on deposit, and must exercise such rights in accordance with investors' directions.¹¹⁴

5 Performance

Demand for Shanghai – Hong Kong Stock Connect has been volatile during its first six months. On the first day of trading, the Northbound daily quota of RMB 13 billion was exhausted by early afternoon but the Southbound link used less than 20% of its daily quota. During the following month, trading interest subsided, with daily Northbound trading hovering below RMB 3 billion. Southbound transactions amounted to less than RMB 300 million daily. Sentiment turned sour as Stock Connect failed to live up to its pre-launch expectations.¹¹⁵ In an attempt to boost demand, in late March 2015, the CSRC extended the trading-link to include mutual funds, which had previously been excluded from the programme.¹¹⁶ Well received by the market, southbound trading volume surged to HKD 15 billion on 8 April 2015.¹¹⁷

¹⁰⁸ Ibid art 73.

¹⁰⁹ Ibid art 70.

¹¹⁰ Ibid art 67.

¹¹¹ Shanghai Stock Exchange, « 港股通交易与交收 » [Hong Kong Stock Connect Transaction and Settlement] <<http://edu.sse.com.cn/col/shhkconnect/faq/jyyjs/>>.

¹¹² CSRC Provisions, above n 92, art 13.

¹¹³ Ibid.

¹¹⁴ Ibid.

¹¹⁵ « 沪港通启动仓促 不尽人意 » [Shanghai-Hong Kong Stock Connect Launched in Rush led to Underperformance], 华尔街日报中文 *Wall Street Journal Chinese Edition* (China), 18 February 2015.

¹¹⁶ « 公开募集证券投资基金参与沪港通交易指引 » [Guidance for Publicly Raised Securities Investment Fund to Participate in Shanghai-Hong Kong Stock Connect] (People's Republic of China) China Securities Regulatory Commission, Order No 5 [2015], 27 March 2015.

¹¹⁷ Josh Noble, 'HK-Shanghai Stock Trading Link Activity Surges' *Financial Times* (online), 8 April 2015 <<http://www.ft.com/intl/cms/s/2/f363f7a2-dda4-11e4-bc0d-00144feab7de.html#axzz3eVPGaRAX>>.

It is early days for the Shanghai – Hong Kong Stock Connect, too early to determine whether it is a success or not.¹¹⁸ Charles Li, Chief Executive of HKEx, emphasised that investors should pay more attention to the long-term impact of the programme rather than on its short term performance.¹¹⁹ Mr Li also defended the value of Shanghai-Hong Kong Stock Connect and Shenzhen – Hong Kong Stock Connect (in progress) by stressing the “bridging” function of the programmes and low transaction costs.¹²⁰ To increase the attractiveness of the Stock Connect programmes, the plan is to expand them to include a wider variety of products such as stock index futures, commodity and fixed-income products.¹²¹

BlackRock recently announced that it was planning to invest USD60 million in the purchase of A-shares through Shanghai-Hong Kong Stock Connect.¹²² However, the sharp declines in A-share and H-share markets during July 2015 has led to net outflows (where selling exceeds buying) in both trading directions of the Shanghai-Hong Kong Stock Connect.¹²³

¹¹⁸ Kevin Martin, ‘Slow Start for Shanghai – Hong Kong Stock Connect is No Indicator of Its True Potential’ *Southern China Morning Post* (online), 15 December 2014 <<http://www.scmp.com/comment/insight-opinion/article/1661459/slow-start-shanghai-hong-kong-stock-connect-no-indicator-its>>.

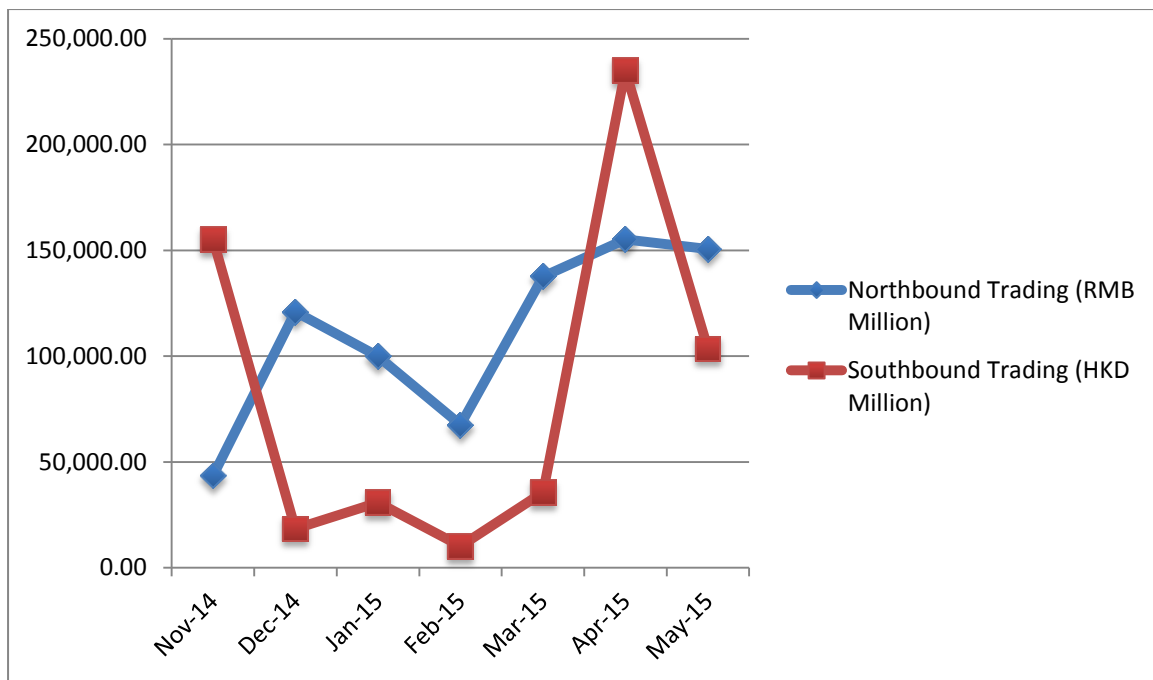
¹¹⁹ Josh Noble, ‘Demand for China’s Stock Connect Slumps’, *Financial Times* (online), 19 November 2014 <<http://www.ft.com/cms/s/0/e138d20e-6fc8-11e4-90af-00144feabdc0.html#ixzz3Z2rr59zs>>.

¹²⁰ 邬川 [Wu Chuan], «港交所总裁：沪港通这座“桥”我死了都不能拆» [HKEx CEO: Shanghai-Hong Kong Stock Connect is a Bridge That Should Not Be Demolished], «腾讯财经» [Tencent Finance], 27 June 2015 <<http://finance.qq.com/a/20150627/016035.htm>>.

¹²¹ «李小加：金融市场双向开放“组团游” 下一站深港通» [Charles Li: Financial Market Opens Up in Both Directions Next Stop is Shenzhen-Hong Kong Stock Connect] «腾讯财经» [Tencent Finance], 29 June 2015 <<http://money.163.com/15/0629/01/AT88AMFT00253B0H.html>>.

¹²² «外资入场！贝莱德借沪港通抄底中国 A 股» [Foreign Investment Enters the Market! BlackRock Uses Shanghai-Hong Kong Stock Connect to Purchase Chinese A- Shares] «凤凰财经» [Phoenix Finance], 30 June 2015 <http://finance.ifeng.com/a/20150630/13807272_0.shtml>.

¹²³ «沪港通双向均现净卖出» [Net Outflow for Shanghai-Hong Kong Stock Connect Both Directions] «凤凰财经» [Phoenix Finance], 30 June 2015 <http://finance.ifeng.com/a/20150630/13807027_0.shtml>.



Turnover based on the data published by HKEx.

(<http://www.HKEx.comhk/eng/csm/>)

5 Differences in Trading Rules

Chinese settlement and clearing rules require sellers of A-shares to deliver their shares to brokers on the day prior to the sale for pre-trade checking. This requirement creates additional counterparty risk for investors selling A-shares in Hong Kong and has been raised as one of the major concerns that deters investors from entering the scheme. HKEx addressed this concern by implementing a new mechanism that permits investors to meet the pre-trade checking requirement without transferring their shares to brokers before sale. Under the arrangement, investors can open a Special Segregated Account (SPSA) in CCASS. Shares are transferred into the SPSA for the purpose of meeting the pre-trade checking requirement.¹²⁴

Day trading of SSE shares is prohibited hence Hong Kong and international investors cannot sell SSE shares before delivery.¹²⁵ In contrast, Hong Kong shares bought under Stock Connect can be sold before delivery once the purchase transaction is confirmed.¹²⁶

6 Cross-Border Regulatory Cooperation and Investors Protection

¹²⁴ Hong Kong Exchanges and Clearing Limited, *General Rules of CCASS*, above n 103, r 4104A.

¹²⁵ Shanghai Stock Exchange, *Measures for Pilot Program*, above n 89, art 31. Note: SSE adopts T+1 model under which shares are settled one day after the trade.

¹²⁶ Ibid art 67.

SSE and HKEx each regulate and supervise their own listed companies and market participants. In the event of cross-boundary market irregularities under the Stock Connect, the SSE or HKEx can request the other exchange to conduct an investigation into the suspected misconduct and impose disciplinary sanctions.¹²⁷ Nevertheless, the operative principle is that investors look to the regulator of the market in which they have traded for protection.¹²⁸ Investors are entitled to bring civil proceedings for compensation and to enforce judgments through bilateral judicial assistance mechanism.¹²⁹

The CSRC and SFC have signed a Memorandum of Understanding to further enhance their regulatory and enforcement cooperation under the Stock Connect.¹³⁰ The memorandum establishes mechanisms for cooperation with respect to alerts, exchange of investigatory information, investigations, use of information, service of documents and execution of judgments.

7 No Protection under Investor Compensation Fund

Shanghai-Hong Kong Stock Connect investors in Hong Kong, however, are not covered by the Hong Kong's Investor Compensation Fund (which only covers financial loss caused by the default of a licensed entity or authorised institution dealing in publicly traded financial products in Hong Kong). Under the Stock Connect, Southbound trading is carried out by mainland China securities firms which are not licensed with the SFC and the Northbound trading relates to shares listed in SSE. Trading in either direction thus falls outside the scope of the Hong Kong compensation fund. Similarly, Hong Kong investors are not protected by the China Securities Investor Protection Fund because the trades are conducted by Hong Kong brokers rather than mainland China brokers. The lacklustre performance of the Shanghai-Hong Kong Stock Connect may, in part, be attributable to this lack of investor protection for trades. This is likely an oversight in the programme which could be easily rectified.

D Market Data Vendor Licence Agreement between SSE and HKEx (2015)

¹²⁷ Ibid.

¹²⁸ China Securities Regulatory Commission, *Press Conference on April 11 2014* (11 April 2014) <http://www.csrc.gov.cn/pub/csrc_en/newsfacts/PressConference/201404/t20140418_247242.html>.

¹²⁹ Ibid.

¹³⁰ China Securities Regulatory Commission and the Securities and Futures Commission of Hong Kong, *Memorandum of Understanding between the CSRC and SFC on Strengthening of Regulatory and Enforcement Cooperation Under Shanghai-Hong Kong Stock Connect*, above n 84.

In March 2015, HKEx Information Services Limited and SSE Infonet, the wholly-owned information business subsidiaries of HKEx and SSE, respectively, entered into a market data vendor licence agreement designed to meet the demand of mainland investors for Hong Kong market data. The agreement allows SSE Infonet to provide mainland China brokerages and retail investors with real-time data from the Hong Kong market.¹³¹

E China Securities Index Limited (CSI) (2005)

CSI is a joint venture established by the SSE and SZSE in 2005 to specialise in the creation and management of indices and index-related services. CSI aims to promote financial innovation by capitalising on the technical expertise of the two exchanges and is becoming the leading index provider in China.¹³²

CSI maintains a wide range of indices based on factors such as size, sector, style, strategies and others. CSI 300 is the first index launched by SSE and SZSE together. It reflects the price fluctuations and performance of the Chinese A-share market. The index is designed for use as a performance benchmark as well as providing the basis for derivatives innovation and indexing.¹³³

F China Exchanges Services Company Limited (CESC)(2012)

In September 2012, HKEx, SSE and SZSE created the China Exchanges Services Company Limited (CESC), a joint venture registered and incorporated in Hong Kong with a combined capitalisation of HKD300 million; HKEx, SSE and SZSE are equal partners. The formal goals of CESC are to promote collaboration among the three stock exchanges in furtherance of the internationalisation of China's capital markets.¹³⁴ CESC's principal businesses include compiling cross-border indices based on products traded on the Hong Kong and mainland China securities markets, developing industry classifications for listed companies, and developing information standards and information products. CESC also develops financial products to link mainland China and Hong Kong markets with global investors.¹³⁵

¹³¹ Hong Kong Exchanges and Clearing Limited, 'Subsidiaries of HKEx and SSE Sign Market Data Vendor Licence Agreement' (News Release, 30 March 2015) <<http://www.hkex.com.hk/eng/newsconsul/HKExnews/2015/150330news.htm>>.

¹³² China Securities Index Co Ltd, *Brief Introduction* (2013) <http://www.csindex.com.cn/sseportal_en/csiportal/gywm/gsjjs.jsp>.

¹³³ China Securities Index Co Ltd, *CSI Indices* (2013) <http://www.csindex.com.cn/sseportal_en/csiportal/zs/indexreport.do?type=1>.

¹³⁴ China Exchanges Services Company Limited, *About CESC* <<http://www.cesc.com/en/About-Cesc/Company-Profile.html>>.

¹³⁵ Ibid.

The Board of CESC consists of nine members with HKEx, SSE and SZSE each having equal representation. A triumvirate of Chief Executive and two Deputy Executives is responsible for the management of CESC.¹³⁶

1 CES China Cross-Border Index Series

A series of cross-border price performance equity indices exist: the CES China 120 Index (CES 120), CES A80 Index (CES A80), CES China HK Mainland Index (CES HKMI) and CES China 280 Index (CES 280). CES China 120 consists of the 80 most liquid and largest stocks by market value trading in Shanghai and Shenzhen, as well as the 40 most liquid and largest mainland Chinese companies (in terms of market value) listed in Hong Kong. The CES 120 is denominated in RMB and calculated in real-time during the trading hours of any of the exchanges on which an index constituent is listed.¹³⁷ The CES A80 represents the A-share portion of the CES 120. It includes the 80 most liquid and largest stocks listed on the SSE and SZSE. The CES A80 is also denominated in RMB and calculated in real-time during the trading hours of SSE and SZSE.¹³⁸ Among Hong Kong-listed mainland Chinese companies in the CES 120, the CES HKMI is comprised of the 40 most liquid and largest. Constituents of the CES HKMI must be mainland based, either by virtue of being registered or having their operations centred there or generating more than 50 % of their revenue from mainland China. The CES HKMI is denominated in HKD and calculated in real-time during the trading hours of HKEx.¹³⁹ Lastly, the CES 280 draws from both mainland and Hong Kong listed shares. From the SSE and SZSE, the 200 largest A-share companies ranked after the constituents of the CES A80 are included as well as the 80 largest HKEx mainland companies, ranked after the constituents of the CES HKMI. The CES 280 is denominated in RMB and calculated in real-time during the trading hours of any of the exchanges on which an index constituent is listed.¹⁴⁰

2 CES Shanghai-Hong Kong Stock Connect Index Series

This is a new series of indices launched in December 2014 in response to the Shanghai-Hong Kong Stock Connect. It consists of the CES Shanghai – Hong Kong Stock Connect 300 Index (CES SHSC 300) and the CES Stock Connect Hong Kong Select 100 Index (CES

¹³⁶ Ibid.

¹³⁷ China Exchanges Services Company Limited, *Product* <<http://www.cesc.com/en/Product.html>>.

¹³⁸ Ibid.

¹³⁹ Ibid.

¹⁴⁰ Ibid.

SCHK 100). The former is designed to track the overall performance of both markets. It is comprised of the top 200 SSE-listed A-shares which are eligible for the Stock Connect and the top 100 Stock Connect eligible stocks listed on HKEx. The latter includes the top 100 HK-listed shares which are eligible for Stock Connect, excluding the dual-listed A- and H-shares. It is designed to provide mainland investors with more information on the performance of HKEx listed shares under Stock Connect.¹⁴¹

3 Product Licencing Business

China Exchanges Service Company Limited (CES) grants licences for developing Hong Kong listed derivatives based on its indices. Hong Kong and international investors gain exposure to mainland companies' shares listed in the three exchanges through these CES Index-linked products. Currently, there are three CES Index-linked ETFs and one CES Index-linked derivatives listed on SEHK.¹⁴²

IV THE FUTURE

A Shenzhen – Hong Kong Stock Connect

1 The Official View

During his trip to Shenzhen in January 2015, Premier Li Keqiang signalled that Shenzhen – Hong Kong Stock Connect should be the next step in furthering the Stock Connect system. Zhang Xiaojun, the spokesperson for the CSRC, commented in a press conference in late April 2015 that Shenzhen – Hong Kong Stock Connect would be at the top of the agenda for the CSRC in 2015.¹⁴³ The CEO of HKEx, Charles Li, indicated that the HKEx would complete its preparation for Shenzhen – Hong Kong Stock Connect by July 2015.¹⁴⁴ Various unofficial sources have suggested that the State Council has approved the Proposal for

¹⁴¹ Ibid.

¹⁴² The CES Index-linked ETFs are ChinaAMC CES China A80 Index ETF, CSOP CES China A80 ETF and E Fund CES China 120 Index ETF. The CES Index-linked derivatives are featured in the CES China 120 Index Futures.

¹⁴³ 叶紫君 [Ye Zijun], «证监会:深港通将是今年主要工作» [CSRC: Shenzhen-Hong Kong Stock Connect Will Be the Major Project for 2015] «华尔街见闻» [Wall Street Journal China Edition] (online), 30 April 2015 <<http://wallstreetcn.com/node/217459>>.

¹⁴⁴ 苏晓 [Su Xiao], «港交所:“深港通”7月底完成准备» [HKEx: Preparation for Shenzhen-Hong Kong Stock Connect to be Completed by July] «搜狐新闻» [Sohu News] (online), 24 June 2015 <<http://news.sohu.com/20150624/n415517264.shtml>>.

Shenzhen – Hong Kong Stock Connect in early May and the programme is expected to roll out during 4th quarter of 2015.¹⁴⁵

During a visit to the HKEx by SZSE delegates in February 2015, the director of SZSE explained the three fundamental principles in designing the Shenzhen – Hong Kong Stock Connect: (1) the basic framework and structure would be the same as that of the Shanghai-Hong Kong Stock Connect; (2) the number of eligible shares to be traded under the Shenzhen – Hong Kong Stock Connect may increase based on the experience of Shanghai – Hong Kong Stock Connect; (3) the programme would be responsive to the market.¹⁴⁶

2 Market Expectations

The financial community has expressed more excitement and higher expectations for the Shenzhen – Hong Kong Stock Connect than for its Shanghai sibling. Geographic proximity has led to extensive interaction and cooperation between Hong Kong and Shenzhen over the years, promoting greater mutual understandings and cooperation between the two markets.¹⁴⁷ Furthermore, unlike the Shanghai Stock Exchange which is home to many state-owned enterprises, the SZSE has become the destination for dynamic, new, small to medium-sized companies (SMEs) in the IT and software development sector.¹⁴⁸ With wider industry coverage and more listings than Shanghai, the SZSE provides a more diverse pool of securities for investors with different risk preferences.¹⁴⁹

It has been suggested that if the mission of the Shanghai – Hong Kong Stock Connect is to ‘connect’ the two markets, the Shenzhen – Hong Kong Stock Connect should strive to ‘integrate’ the Shenzhen and Hong Kong market.¹⁵⁰ Bolder measures may be adopted for the Shenzhen--Hong Kong Stock Connect, such as reducing or eliminating the minimum asset

¹⁴⁵ ‘消息称深港通已获国务院批 细则最快月内公布 [Shenzhen-Hong Kong Stock Connect Obtained State Council Approval Detailed Guidelines Expected to Be Released within the Month]’, «新浪财经» [Sina Finance] (online), 5 May 2015 <<http://finance.sina.com.cn/stock/hkstock/hkstocknews/20150508/080322134126.shtml>>.

¹⁴⁶ 深圳证券交易所 [Shenzhen Stock Exchange], ‘深圳证券交易所吴利军理事长一行访港推进深港合作 [Director of Shenzhen Stock Exchange Visited the HKEx to Promote Cooperation with Shenzhen and Hong Kong]’ (News Release, 2 February 2015) <<http://www.szse.cn/main/aboutus/bsyw/39753935.shtml>>.

¹⁴⁷ 梁海明 [Liang Haiming], “‘深港通’不能再局限于‘通’ [Shenzhen-Hong Kong Stock Connect Cannot Be Limited to ‘Connect’ Only]”, *Financial Times Chinese Edition* (online), 24 March 2015 <<http://www.ftchinese.com/story/001061189>>.

¹⁴⁸ Mark Austen, ‘Comment: Shenzhen Next Stop on Through Train’, *Financial Times* (online), 26 January 2015 <<http://www.ft.com/intl/cms/s/0/e52fd4bc-a492-11e4-b943-00144feab7de.html#axzz3ZdkZ329b>>.

¹⁴⁹ Ibid.

¹⁵⁰ 梁海明 [Liang Haiming], above n 147.

threshold requirement applicable to Southbound investors or expanding eligible shares to include SME and GEM shares from both markets.¹⁵¹

B Qianhai Shenzhen – Hong Kong Modern Service Industry Cooperation Zone

1 Background

The Qianhai Shenzhen – Hong Kong Modern Service Industry Cooperation Zone (the Cooperation Zone) is an experimental zone approved by the State Council of mainland China for developing a modern service sector and increasing cooperation between mainland China and Hong Kong.¹⁵² More significantly, it is anticipated that the Cooperation Zone will be a pioneer in financial system reforms and innovation; its mandate is to serve as an example of the opening up of the Chinese financial industry.¹⁵³ The Cooperation Zone Working Plan also envisages innovative and deepening cooperation between SZSE and HKEx within the Cooperation Zone itself.¹⁵⁴ The Qianhai Management Bureau announced its plan to build a financial innovation centre with the support of both Shenzhen and Hong Kong exchanges, including exploring the feasibility of establishing a stock exchange with an offshore international board.¹⁵⁵

¹⁵¹ Ibid.

¹⁵² *Reply of the State Council on the Relevant Policies Supporting the Development and Opening-up of the Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone* (People's Republic of China) State Council of the People's Republic of China, Order No 58, 27 June 2012, art1.

¹⁵³ Ibid art 2.

¹⁵⁴ «前海深港现代服务业合作区促进深港合作工作方案» [Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone Promoting Shenzhen-Hong Kong Cooperation Working Plan] (People's Republic of China) Shenzhen Qianhai Management Bureau, 4 December 2014, art 24.

¹⁵⁵ ‘自贸区 2.0 版全面启动 前海探索开设离岸国际板 [Free Trade Zone Version 2.0 Fully Launched Qianhai Considering Establishing Offshore International Board]’, 新华网 [XinHua Net] (online), 28 April 2015 <http://news.xinhuanet.com/finance/2015-04/28/c_127740544.htm>.



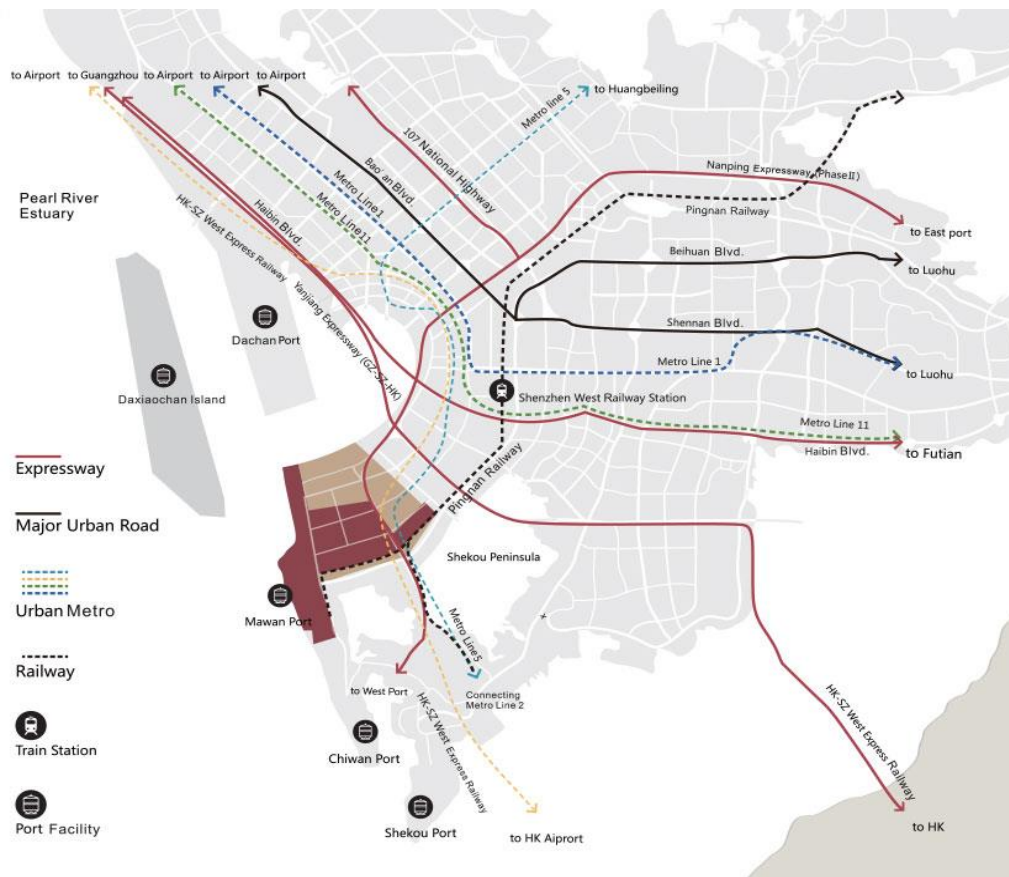
(Photo: Source from Internet

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<http://bbs.szhome.com/commentdetail.aspx?id=150513303&projectid=430300&uid=1733250&page=1>>)

The Cooperation Zone is located at the intersection of a major regional development axis and the coastal expansion zone of the Pearl River Delta. Qianhai is close to airports in both Shenzhen and Hong Kong. The Shenzhen-Zhongshan Cross-river Pathway, Shenzhen West Port Area and Shenzhen North Railway Station all connect to Qianhai, with the Guangzhou-Shenzhen Riverside Expressway alongside. One hour to the Pearl River Delta and half-an-hour to Hong Kong, Qianhai is of great strategic significance to both Guangdong and Hong Kong. It boasts convenient sea, land and air transport as well as prominent comprehensive transport advantages.¹⁵⁶

¹⁵⁶ Qianhai Shenzhen – Hong Kong Modern Service Industry Cooperation Zone, *Transportation* (2015) <http://www.szqh.com.cn/What_is_Qianhai/Transportation/>.



2 Legal Environment

The goal of Qianhai is to create a legal system which draws from both mainland China and Hong Kong, supported by three new legal institutions: the Shenzhen Court of International Arbitration, the Qianhai Tribunal and the Qianhai Anti-Corruption Bureau.¹⁵⁷ Qianhai Anti-Corruption Bureau, as its name indicates, provides anti-corruption supervision within the Cooperation Zone. The Qianhai Tribunal is running a pilot programme experimenting with the use of a 'Single Judge Trial + Mediation Council + Hong Kong Jury + Professional Judgement' in an attempt to provide a western-style jury system together with a Chinese-style mediation system. The Tribunal selects Chinese nationals holding Hong Kong citizenship to serve as members of the jury.¹⁵⁸ The Shenzhen Court of International Arbitration was officially launched in Qianhai with a registry of 180 foreign arbitrators, accounting for 35%

¹⁵⁷ Qianhai Shenzhen – Hong Kong Modern Service Industry Cooperation Zone, *Legal Environment* (2015) <http://www.szqh.com.cn/Why_Qianhai/Legal_Environment/>.

¹⁵⁸ Ibid.

of all arbitrators in Qianhai. Parties can adopt applicable laws of other jurisdictions and appoint lawyers from Hong Kong, Macau, Taiwan or elsewhere.¹⁵⁹

The Ministry of Finance has approved a proposal to permit Qianhai-Guangdong-Hong Kong – Macau law firms to provide legal services. Hong Kong law was chosen as the applicable law in the draft “Guidelines on Hong Kong-related Contracts for the Shenzhen Special Economic Zone and the Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone”. Efforts are now being made to solicit the support of the National People’s Congress.¹⁶⁰

C Demutualisation of SSE and SZSE

The old-fashioned membership structure of SSE and SZSE has undermined the attractiveness of Chinese stock exchanges for companies in high growth industries.¹⁶¹ Some of the largest Chinese IT companies, such as Alibaba, JingDong(JD), Tencent, have chosen to list on HKEx, NASDAQ or NYSE instead of SSE or SZSE. SSE and SZSE were established with support from both government and market participants. They have been described as ‘administrative membership-based exchanges’ because their organisation structure and decision making mechanism are subject to CSRC’s supervision and control.¹⁶² In a mutual membership based association the Members’ Meeting is the ultimate decision making body. However, in the case of SSE and SZSE, the regulator, the CSRC, and the State Council, dominate the decision-making process. The mainland Chinese exchanges are, in fact, government affiliated organisations that execute government policies and implement national laws and regulations at the direction of government.¹⁶³ Of course, this is consistent with the macroeconomic objectives of capital markets regulation in mainland China; these exchanges are not creatures of the market.

But this organisational structure of the mainland exchanges has resulted in delayed responses to market information and even decisions contrary to market imperatives.¹⁶⁴ Demutualisation and corporatisation, currently the most usual (although not exclusive) structure worldwide

¹⁵⁹ Ibid.

¹⁶⁰ Ibid.

¹⁶¹ 卢晶，刘晓东 [Lu Jing, Liu Xiaodong], ‘中国证券市场优质上市公司资源流失与沪深交易所制度改革探析 [Loss of Good-Quality Listed Companies in China Securities Market and Exploring Reform to Shanghai and Shenzhen Stock Exchanges]’ (2014) 12 商业经济 *Commercial Economics* 117, 117-119.

¹⁶² Ibid.

¹⁶³ Ibid.

¹⁶⁴ Ibid.

would, the argument goes, generate external incentives for the stock exchanges to enhance efficiency and competitiveness.¹⁶⁵

D Merger of SSE, SZSE and HKEx

Waves of stock exchange mergers, primarily in Europe, have prompted discussion about the potential of creating one single China Stock Exchange by merging SSE and SZSE. However, former SSE Chairman, Gengliang, saw no significant benefit to be derived from such a merger for two reasons. First, because SSE and SZSE products largely overlap, there would be no competitive advantage resulting from complementarity. Secondly, the merger would reduce competition and the ability of investors to negotiate transaction fees (in fact, a somewhat illusory power).¹⁶⁶

A more ambitious plan of consolidating all three exchanges, SSE, SZSE and HKEx, was widely discussed in 2011, at a time several high profile international mergers appeared to be in the offing.¹⁶⁷ Practical and technical difficulties quickly ended such speculation. For one thing, the SSE and SZSE membership-based organisation structure was incompatible with the publicly listed HKEx. At the time, China's capital account restrictions, now gradually easing, prevented seamless cross border settlement. Demutualisation of the mainland exchanges would address the first impediment, but at the cost of state control, a politically unpalatable consequence.

Within a generation, it is certainly not impossible to envisage a single China Stock Exchange, into which would be rolled SSE, SZSE and HKEx. The political and economic integration of Hong Kong and mainland China continues apace, a geopolitical inevitability. For the time being however, the three exchanges serve different purposes and operate in large dynamic economies which can support each of them individually. The political forces of convergence and coordination are strong though, so short of formal merger, the exchange habitats, the infrastructure, the systems, the supporting institutions, are being groomed for the future through cooperative accords and initiatives.

¹⁶⁵ Ibid.

¹⁶⁶ 阳帆 [Yang Fan], '全球交易所并购潮下的中国思索 [China's Perspective on the Global Trend of Stock Exchanges Consolidation]' (2011) 6 金融家 *Financier* 121, 121-122.

¹⁶⁷ Singapore was in negotiations with Sydney and London with Toronto, for example. These mergers did not go forward.

Part F Timelines – Dancing to the Merger Music

F.1 Euronext NYSE ICE

I EURONEXT (PRE-NYSE)

- 22 September 2000** Euronext is formed after the merger of Brussels Stock Exchange, Paris Bourse and Amsterdam Exchanges¹, creating a single trading platform for companies to trade, despite maintaining the three venues. The price of stock is the same across all venues and company can choose which venue to trade.²
- 5 July 2001** Euronext successfully completes its IPO. Euronext shares are first traded on the Premier Marché of Euronext Paris until a unified platform is created. The total market capitalisation is EUR 693 million, comprising 16.7 million new shares and 12.2 million existing shares. The new shares are priced at EUR 24 per share. The shares are sold mainly to international institutional investors. A public offering is conducted to retail investors in France, Belgium and Netherlands and is oversubscribed.³
- October 2001** Euronext secures LIFFE after winning LSE over the battle.⁴ Despite a higher cash and share offer from LSE, Euronext beats its rivals with an all-cash bid of £555 million, or £18.25 per share, and promises to retain LIFFE's management and its platform, despite higher cash-and-share offer from LSE.⁵
- January 2002** Euronext includes the Portuguese exchange Bolsa de Valores de Lisboa e Porto. BVLP's shareholders unanimously accept Euronext's merger offer.⁶ BVLP merges with Euronext and becomes a wholly-owned subsidiary of Euronext NV and is renamed Euronext Lisbon. Euronext issues 4.8 million new shares and pays EUR 35 million in cash in exchange for the six million BVLP shares from BVLP's original

¹ Euronext, *Brussels* <<https://www.euronext.com/en/markets/nyse-euronext/brussels>>.

² James McAndrews and Chris Stefanadis, 'The Consolidation of European Stock Exchanges' (2002) 8(6) *Current Issues in Economics and Finance* 1, 2.

³ Phillipa Leighton-Jones and Luke Jeffs, 'The Road to Consolidation – An Exchange Merger Timeline', *Financial News* (online), 15 February 2008 <<http://www.efinancialnews.com/story/2008-02-15/the-road-to-consolidation-an-exchange-merger-timeline-1?ea9c8a2de0ee111045601ab04d673622>>; 'Euronext IPO Successfully Completed – IPO Price: EUR 24 per Share', *Mondo Visione* (online), 5 July 2001 <<http://www.mondovisione.com/news/euronext-ipo-successfully-completed-ipo-price-eur-24-per-share/>>.

⁴ 'Liffe Chiefs Back Euronext Bid', *BBC News* (online), 29 October 2001 <<http://news.bbc.co.uk/2/hi/business/1626392.stm>>.

⁵ Ibid; George Trefgarne, 'LSE Bid Spurned as Liffe Prefers French', *The Telegraph* (online), 30 October 2001 <<http://www.telegraph.co.uk/finance/markets/2739795/LSE-bid-spurned-as-Liffe-prefers-French.html>>.

⁶ 'BVLP Joins Euronext', *Mondo Visione* (online), 30 January 2002 <<http://www.mondovisione.com/news/bvlp-joins-euronext/>>.

shareholders.⁷

II NYSE EURONEXT

- 1 June 2006** Euronext and NYSE announce and sign an agreement for a merger of equals. A new entity – NYSE Euronext – is formed and its shares, denominated in U.S. dollars and Euros, are sold on both the NYSE and Euronext Paris exchanges.⁸
- 27 November 2006** Both NYSE and Euronext obtain approval from the Securities and Exchange Commission in relation to the merger, with the condition attached to the approval requiring approval of shareholders from both entities.⁹
- 19 December 2006** Euronext shareholders approve the merger with NYSE Group.¹⁰
- 20 December 2006** 99.7% of NYSE Group shareholders vote in favour of the merger.¹¹
- 15 February 2007** NYSE Euronext commences offer for Euronext shares. The standard offer is that Euronext shareholders receive €21.32 in cash and 0.98 of a share of NYSE Euronext common stock for each Euronext share owned.¹²
- 27 March 2007** NYSE Euronext completes its offer to Euronext shareholders and the process is successful with 91.4% of Euronext's share capital and 92.2% of voting rights tendered.¹³
- 4 April 2007** NYSE Euronext is formed.¹⁴
- 11 May 2008** NYSE Euronext announces the signing of a Memorandum of Understanding (MOU) to develop a long term partnership with the Zhengzhou Commodity Exchange to develop futures and options as

⁷ 'BVLP Shareholders Agree Euronext Merger', *Fin Extra* (online), 31 January 2002 <<http://www.finextra.com/news/fullstory.aspx/fullstory.aspx?newsitemid=4587>>.

⁸ NYSE, 'NYSE Group and Euronext Announce Merger' (News Briefs, June 2006) <<http://www1.nyse.com/about/publication/1145959806931.html>>.

⁹ Ibid.

¹⁰ Aaron Lucchetti and Alistair MacDonald, 'Euronext Holders Approve Deal for Historic Merger with NYSE', *The Wall Street Journal* (online) <<http://www.wsj.com/articles/SB116653086274154451>>.

¹¹ NYSE, 'NYSE Group Shareholders Overwhelmingly Approve Combination with Euronext, Preliminary Results Indicate — Approximately 99.7 Percent of Voting Shareholders in Favor of Merger' (News Release, 20 December 2006) <<http://www1.nyse.com/press/1166613560168.html>>.

¹² NYSE, 'NYSE Euronext to Commence Offer for Euronext Shares' (News Release, 15 February 2007) <<http://www1.nyse.com/press/1171453128510.html>>.

¹³ NYSE, 'NYSE Euronext Offer for Euronext Shares Is Successful: Euronext Shareholders Tender 91.4% of Their Shares in the Friendly Offer Initiated by NYSE Euronext' (News Release, 27 March 2007) <<http://www1.nyse.com/press/1174947115311.html>>.

¹⁴ NYSE, *Timeline* (2014) <http://www1.nyse.com/about/history/timeline_events.html>.

part of the exchange's major expansion in Asia, in particular China.¹⁵

- 1 October 2008** NYSE Euronext acquires the American Stock Exchange (Amex).¹⁶ It becomes the third largest U.S. options marketplace.¹⁷ Under the agreement, Amex receives \$260 million in NYSE Euronext common stock, plus additional shares of NYSE Euronext common stock based on the net proceeds from the expected sale of Amex's lower Manhattan headquarters.¹⁸ The exchange then became known as NYSE Alternext US and NYSE Amex LLC in the past¹⁹ and now the current name is NYSE MKT LLC.²⁰
- 29 January 2009** NYSE Euronext launches the New York Block Exchange (NYBX) with BIDS Trading under a joint venture agreement. The exchange is a new innovative platform to allow access to both displayed and reserve liquidity of the NYSE order book.²¹ The NYBX operation is cleared by the U.S. Securities and Exchange Commission on 26 January 2009.²² It will operate as a facility of NYSE and be accessible via BIDS Trading and open to all NYSE members.²³
- 19 June 2009** NYSE Euronext signs a deal with the State of Qatar to form a strategic partnership. NYSE Euronext invests \$200 million for a 20 percent stake of the new exchange.²⁴ NYSE Euronext and Qatar Holding rebrand the Doha Securities Market as the Qatar Exchange".²⁵ The exchange uses the NYSE Euronext technology - Universal Trading Platform (UTP) - for its cash and derivatives markets.²⁶
- 18 June 2009** NYSE Euronext and The Depository Trust & Clearing Corporation (DTCC) agree to create a joint venture for clearing U.S. fixed income

¹⁵ NYSE, 'NYSE Euronext, Zhengzhou Commodity Exchange Announce Memorandum of Understanding Exchanges Enter into Agreement to Develop Futures and Options Markets in US and China' (News Release, 5 November 2008) <<http://www1.nyse.com/press/1226056139390.html>> quoted in 'Zhengzhou Commodity Exchange Announce Memorandum of Understanding – Exchanges Enter into Agreement to Develop Futures and Options Markets in US and China', *Mondo Visione* (online), 11 May 2008 <<http://www.mondovisione.com/media-and-resources/news/nyse-euronext-zhengzhou-commodity-exchange-announce-memorandum-of-understanding-/->>.

¹⁶ NYSE, 'NYSE Euronext Completes Acquisition of American Stock Exchange' (News Release, 1 October 2008) <<http://www1.nyse.com/press/1222772889985.html>>.

¹⁷ NYSE, *Timeline*, above n 14.

¹⁸ NYSE, 'NYSE Euronext to Acquire the American Stock Exchange' (News Release, 17 January 2008) <<http://www1.nyse.com/press/1200568235016.html>>.

¹⁹ NYSE, 'SEC Approves Name Change of NYSE Alternext US to NYSE Amex' (New Release, 18 March 2009) <<http://www1.nyse.com/press/1237371839728.html>>.

²⁰ NYSE, 'NYSE Amex LLC to Be Renamed NYSE MKT LLC' (News Release, 4 May 2012) <<http://www1.nyse.com/press/1336646911531.html>>.

²¹ NYSE, 'New York Block Exchange Officially Launches Today' (News Release, 29 January 2009) <<http://www1.nyse.com/press/1233227663062.html>>.

²² NYSE, 'NYSE Euronext and BIDS Trading Receive SEC Approval to Launch the New York Block Exchange' (News Release, 26 January 2009) <<http://www1.nyse.com/press/1232969873591.html>>.

²³ Ibid.

²⁴ NYSE, 'The State of Qatar Launches "Qatar Exchange" as It Signs Today Formal Terms of Strategic Partnership with NYSE Euronext' (News Release, 19 June 2009) <<http://www1.nyse.com/press/1245406656784.html>>.

²⁵ Ibid.

²⁶ Ibid.

derivatives. The new clearing house New York Portfolio Clearing (NYPC) offers risk management, clearing and settlement for U.S. fixed income securities and derivatives.²⁷

15 February 2011 Deutsche Boerse and NYSE Euronext announce that they are entering into a business combination agreement.²⁸ The proposed deal gives Deutsche Boerse's shareholders 60 percent control and NYSE Euronext shareholders owning the remaining 40%.²⁹ Each share of Deutsche Boerse stock exchanges for 1 share of the new company stock and each share of NYSE Euronext stock exchanges for 0.47 shares of the new company stock.³⁰

1 April 2011 Nasdaq OMX and ICE make a counter-offer to acquire NYSE Euronext for \$11.3 billion.³¹ As part of the proposal, ICE retains NYSE Euronext's derivatives businesses, and NASDAQ OMX retains NYSE Euronext's remaining businesses, including the NYSE Euronext stock exchanges in New York and Europe. ICE and NASDAQ OMX continue to operate as separate businesses.³² NYSE Euronext continues to fend off the repeated takeover attempts from Nasdaq OMX and ICE, maintaining that their counter-offer does not "provide compelling value" and has "unacceptable execution risk."³³ The bid is eventually withdrawn after the federal government of the US threatens to file an anti-trust lawsuit against Nasdaq OMX and ICE.³⁴

7 July 2011 Deutsche Boerse wins shareholder support for its \$9 billion merger with NYSE Euronext, clearing one of the biggest hurdles to the merger. Majority of NYSE Euronext shareholders (over 96%) vote in support of the merger.³⁵ More than 80 percent of the outstanding shares of Deutsche Boerse approve the tender offer.³⁶

1 September 2011 NYSE Euronext acquires provider of high performance market access products Metabit based in Tokyo in an effort to accelerate growth in

²⁷ NYSE, 'NYSE Euronext and BIDS Trading Receive SEC Approval to Launch the New York Block Exchange', above n 22.

²⁸ NYSE, 'Deutsche Boerse AG and NYSE Euronext Agree to Combine to Create the Premier Global Exchange Group' (News Release, 15 February 2011) <<http://www1.nyse.com/press/1297768048707.html>>.

²⁹ Ibid; Ken Sweet, 'NYSE, Deutsche Boerse Agree to Merge', *CNN Money* (online), 15 February 2011 <http://money.cnn.com/2011/02/15/markets/NYSE_exchange_merger/index.htm?iid=EL>.

³⁰ NYSE, 'Deutsche Boerse AG and NYSE Euronext Agree to Combine to Create the Premier Global Exchange Group', above n 28.

³¹ Ben Rooney, 'NYSE Shuns Second Offer from Nasdaq and ICE', *CNN Money* (online), 21 April 2011 <http://money.cnn.com/2011/04/21/news/companies/nyse_rejects_nasdaq_ice_again/index.htm?iid=EL>.

³² Ibid.

³³ Ibid.

³⁴ Aaron Smith, 'Nasdaq and ICE Withdraw NYSE Bid', *CNN Money* (online), 16 May 2011 <http://money.cnn.com/2011/05/16/news/companies/nasdaq_ice_nyse/index.htm?iid=EL>.

³⁵ NYSE, 'NYSE Euronext Shareholders Overwhelmingly Approve Combination with Deutsche Boerse' (News Release, 7 July 2011) <<http://www1.nyse.com/press/1310032901736.html>>.

³⁶ Michael J De La Merced, 'Deutsche Borse Shareholders Approve Deal with NYSE', *The New York Times* (online), 14 July 2011 <http://dealbook.nytimes.com/2011/07/14/deutsche-borse-wins-shareholder-approval-of-nyse-euronext-deal/?_php=true&_type=blogs&ref=nyseeuronext&_r=0>.

Asia-Pacific region. It announces that Metabit will operate as a product line within the NYSE Technologies portfolio whereas the terms of the acquisition are not disclosed.³⁷

- 1 February 2012** The European Commission blocks the merger between NYSE Euronext and Deutsche Boerse on the basis that it will stifle competition by creating a "quasi-monopoly in the area of European financial derivatives traded globally on exchanges."³⁸

III NYSE EURONEXT ICE

- 20 December 2012** The Intercontinental Exchange (ICE) enters into an agreement with NYSE Euronext for its acquisition of NYSE Euronext business. The transaction is priced at \$ 33.12 per NYSE Euronext share and cost about \$8.2 billion.³⁹
- 3 June 2013** ICE shareholders approve the acquisition of NYSE Euronext.⁴⁰
- 24 June 2013** ICE receives European Commission's clearance for NYSE Euronext acquisition.⁴¹
- 3 June 2013** NYSE Euronext approves the sale of the exchange to Intercontinental Exchange Inc.⁴²
- 16 August 2013** The U.S. Securities and Exchange Commission approves the takeover of NYSE Euronext.⁴³
- 13 November 2013** ICE completes the acquisition of NYSE Euronext. ICE particularly targets the LIFFE exchange owned by the NYSE Euronext (acquired by Euronext itself in 2002).⁴⁴ According to the Economists, LIFFE has a large market share in European derivative contracts. It also has a

³⁷ NYSE, 'NYSE Euronext Completes Acquisition of Metabit' (News Release, 1 September 2011) <<http://www1.nyse.com/press/1314874107534.html>>.

³⁸ Aaron Smith, Catherien Tymkiw and Mark M Meinero, 'NYSE-Frankfurt Stock Exchange Merger Blocked', *CNN Money* (online), 1 February 2012 <http://money.cnn.com/2012/02/01/markets/nyse_euronext_deutsche_boerse/>; Aoife White and Nandini Sukumar, 'Deutsche Boerse-NYSE Euronext Takeover Is Blocked by EU', *Bloomberg* (online), 2 February 2012 <<http://www.bloomberg.com/news/articles/2012-02-01/european-commission-blocks-proposed-deutsche-boerse-nyse-euronext-merger>>.

³⁹ IntercontinentalExchange, 'IntercontinentalExchange to Acquire NYSE Euronext for \$33.12 per Share in Stock and Cash, Creating Premier Global Market Operator' (Press Release, 20 December 2012) <<http://ir.theice.com/press-and-publications/press-releases/all-categories/2012/12-20-2012b.aspx>>.

⁴⁰ Ibid.

⁴¹ Ibid.

⁴² 'ICE Buys NYSE-Euronext: The End of the Street', *The Economist* (online), 16 November 2013 <<http://www.economist.com/news/finance-and-economics/21589913-improbable-takeover-highlights-uncertain-future-share-trading-end>>; Kaitlyn Kiernan and Jacob Bunge, 'Investors Approve NYSE Sale to ICE', *The Wall Street Journal* (online), 3 June 2013 <<http://www.wsj.com/articles/SB10001424127887323469804578523132069546530>>.

⁴³ Sarah Lynch and John McCrank, 'SEC Approves ICE's Planned Takeover of NYSE', *Reuters* (online), 16 August 2013 <<http://www.reuters.com/article/2013/08/16/us-ice-nyse-sec-idUSBRE97F0KU20130816>>.

⁴⁴ IntercontinentalExchange, *Fact Sheet* (2014) <https://www.theice.com/publicdocs/ICE_at_a_glance.pdf>.

licence to issue derivatives tied to MSCI share indices and may soon issue other products tied to LIBOR which is administered by another division of ICE.⁴⁵

- 27 May 2014** ICE announces its intention to launch an initial public offering of Euronext N.V. Euronext, after the IPO, regains its independence. Its shares will be traded on Euronext Paris, Euronext Amsterdam, Euronext Brussels and Euronext Lisbon.
- 19 June 2014** Euronext IPO is priced at €20 per share and all of the 42,248,881 offered Shares are sold in the IPO, representing 60.36% of the total issued ordinary share capital of the Company.⁴⁶
- 20 June 2014** Trading of Euronext begins on Euronext Paris, Euronext Amsterdam and Euronext Brussels.⁴⁷

F.2 London Stock Exchange

- July 1998** The LSE and Deutsche Boerse agreed on a strategic alliance.⁴⁸
- May 2000** The LSE and Deutsche Boerse announce their intention to merge to form iX.⁴⁹
- August 2000** OMX, then called OM Group, launches hostile £800m (€1.2bn) bid to buy LSE. It is forced to walk away after amassing just 6.7% of the shares.⁵⁰
- July 2001** The LSE floats at a value of £1bn on its own main market, just six months after Clara Furse joined as chief executive. The bourse celebrates its 200th anniversary as the first regulated exchange in London.⁵¹
- January 2003** The LSE creates EDX London, a new international equity derivatives business, in partnership with OM Group. It also acquires Proquote, a new generation supplier of real-time market data and trading systems.

⁴⁵ 'ICE Buys NYSE-Euronext: The End of the Street', above n 42.

⁴⁶ IntercontinentalExchange, 'IntercontinentalExchange Announces Closing of Euronext Initial Public Offering', (Press Release, 24 June 2014) <<http://ir.theice.com/press-and-publications/press-releases/all-categories/2014/06-24-2014.aspx>>.

⁴⁷ IntercontinentalExchange, 'Euronext IPO Priced at €20 Per Share' (Press Release, 19 June 2014) <<http://ir.theice.com/press-and-publications/press-releases/all-categories/2014/06-19-2014.aspx>>.

⁴⁸ Leighton-Jones and Jeffs, above n 3.

⁴⁹ Ibid

⁵⁰ Ibid

⁵¹ London Stock Exchange, *Our History* (7 July 2015) <<http://www.londonstockexchange.com/about-the-exchange/company-overview/our-history/our-history.htm>>.

Chris Gibson-Smith is appointed chairman.⁵²

- December 2004** Deutsche Boerse makes a bid for the LSE, although its approach is rejected. The new LSE headquarters are opened by the Queen in Paternoster Square, while the group also opens a Hong Kong office. (First Deutsch Boerse attempt)⁵³
- November 2005** A £1.6bn takeover offer from Macquarie Bank is turned down by the LSE, which describes the bid as “derisory”. US exchange operator Nasdaq comes in shortly afterwards with a £2.4bn approach. This too is rejected.⁵⁴
- February 2006** Macquarie Bank walks away from the takeover winning only 0.4% of the shares it needed.⁵⁵
- March 2006** Nasdaq builds a 14.9% stake in the LSE in a bid to gain a foothold in the company in order to take it over. Nasdaq makes its first bid for LSE about £2.9bn of which LSE rejected.⁵⁶
- November 2006** Nasdaq raises its stake in the LSE to 28.75% (according to the Financial Times – Timeline London Stock Exchange). Nasdaq puts in second bid for LSE with a £2.7bn hostile offer. This second bid was rebuffed by LSE chief executive Dame Clara Furse in January 2007. She said: ‘Nasdaq's final offer fails to recognise the outstanding growth record and prospects for our group on a standalone basis let alone the exchange's unique global position’.⁵⁷
- February 2007** Nasdaq finally walks away from the LSE and sells the majority of its stake in LSE to Borse Dubai.⁵⁸
- June 2007** LSE agrees to acquire Borsa Italiana for €1.6billion.⁵⁹
- August 2007** LSE shareholders approve its €1.6bn acquisition of Borsa Italiana. Investors representing 78% of LSE stock vote in favour of the deal. Shareholders controlling 99.9% of Borsa Italiana's stock accept LSE's offer.⁶⁰
- September 2007** Qatar takes a 20% stake of LSE, part of the stake that Nasdaq built up when attempting a hostile takeover, in a deal worth close to £1bn (€1.5bn). Furse makes it clear she does not want a rival bourse to

⁵² ‘London Stock Exchange to Acquire Market Data Services Firm Proquote’, *Finextra* (online), 28 January 2003 <<http://www.finextra.com/news/fullstory.aspx?newsitemid=7854>>.

⁵³ Leighton-Jones and Jeffs, above n 3.

⁵⁴ Ibid.

⁵⁵ Ibid.

⁵⁶ Ibid.

⁵⁷ Lauren Willington, ‘Timeline: London Stock Exchange’, *Financial News* (online), 9 February 2011 <<http://www.efinancialnews.com/story/2011-02-09/lse-timeline-five-years?ea9c8a2de0ee111045601ab04d673622>>.

⁵⁸ Leighton-Jones and Jeffs, above n 3.

⁵⁹ Ibid.

⁶⁰ Ibid.

acquire Nasdaq's holding in the London exchange⁶¹

October 2007	The LSE merges with Borsa Italiana, the Italian stock exchange operator, creating the London Stock Exchange Group. The deal is €1.6bn or worth £1.1bn (from the Financial Times Timeline London Stock Exchange). ⁶² The deal strengthens the LSE's position, making it less prone to takeover targets, changing its shareholder roster. The deal decreases Borse Dubai's stake from 28% to about 22% and the Qatar Investment Authority's holding from 20% to around 14%. The board increases from nine to 12 seats – seven from the LSE, five by Borsa Italiana. ⁶³
June 2008	Clara Furse is committed to launching dark pool Baikal and the LSE takes on Lehman Brothers as a development partner ⁶⁴
October 2008	LSE shocks the market by entering talks to buy Turquoise, a rival to Baikal. ⁶⁵
February 2009	LSE completes acquisition of Turquoise acquiring 60% of Turquoise's shares. ⁶⁶ The Turquoise operation is to consume the operation of Baikal. ⁶⁷ That in effect allows LSE to offer the so-called "dark pool" trading outside of UK and Italy to other countries in Europe. ⁶⁸ David Lester is appointed head of the business, with Eli Lederman and John Wilson, the founder of the LSE's Baikal dark pool, both leaving the group. Baikal and Turquoise, merge into one entity. ⁶⁹
May 2009	The LSE acquires Sri Lanka-based trading technology firm MillenniumIT to develop new systems. ⁷⁰
July 2009	The LSE begins talks with Fortis, the major shareholder in Amsterdam-based clearing house EMCF, over taking its majority stake. ⁷¹
December 2010	Borse Dubai's 20% stake in the LSE and 17% holding in Nasdaq become the target of a \$1.5bn bid from Abu Dhabi's ruling family, who also wants to merge with its bourse, ADX, with DFM, 75% owned by Borse Dubai ⁷²
February 2011	The LSE fails to tie-up an agreed "merger of equals" with Toronto

⁶¹ Ibid.

⁶² Ibid.

⁶³ Willington, above n 57.

⁶⁴ Ibid.

⁶⁵ Ibid.

⁶⁶ Ibid; Jill Treanor, 'London Stock Exchange Takes Rival Turquoise off Bankers' Hands', *The Guardian* (online), 21 December 2009 <<http://www.theguardian.com/business/2009/dec/21/london-stock-exchange-acquires-turquoise>>.

⁶⁷ Treanor, above n 66.

⁶⁸ Ibid.

⁶⁹ Willington, above n 57.

⁷⁰ Ibid.

⁷¹ Ibid.

⁷² Ibid.

bourse operator TMX Group after a consortium of Canadian banks and financial institutions go hostile with a rival C\$2.8bn (£1.8bn) approach. Market observers speculate that the LSE may once again be a takeover target for Nasdaq.⁷³

- July 2013** LSE enters into an agreement to acquire Turquoise Derivatives of Turquoise Global Holdings Limited. Turquoise Derivatives is renamed as “London Stock Exchange Derivatives Market” and operates as part of a Regulated Market of a Recognised Investment Exchange (RIE).⁷⁴ The transaction will be completed during Q4 2013. It is noted that LSE has a 51% in both Turquoise MTF and Turquoise Derivatives. LSE in this transaction only purchases the remaining 49% of Turquoise Derivatives. Turquoise continues to have 49% shares in MTF and be responsible for its operation.⁷⁵
- May 2014** LSE enters talks to purchase Russell Investments in the States. The deal is worth around 2.4 billion US dollars. It will be the largest purchase, if the deal goes through, by the LSE to date.⁷⁶
- July 2014** Qatar Investment Authority sells a third of its stake in LSE before the 1.6bn rights issue to help fund the purchase of Russell. The Qatar retains a 10% stake in LSE.⁷⁷

F.3 Australian Securities Exchange and Singapore Stock Exchange

- 25 October 2010** ASX enters into a merger implementation agreement with SGX for a market value of AUD \$8 billion to create the premier international exchange in Asia Pacific.⁷⁸ The offer comprises of both cash and shares.⁷⁹

⁷³ Ibid.

⁷⁴ London Stock Exchange Group, ‘London Stock Exchange PLC to Acquire Turquoise Derivatives’ (Press Release, 3 July 2013) <<http://www.lseg.com/media-centre/press-releases/news-across-group/london-stock-exchange-plc-acquire-turquoise-derivatives>>.

⁷⁵ Elliott Holley, ‘LSE Launches New Derivatives Market’, *Banking Technology* (online) <<http://www.bankingtech.com/171662/lse-launches-new-derivatives-market>>.

⁷⁶ Philip Stafford, ‘LSE’s Rationale for Buying Russell’, *Financial Times* (online), 20 May 2014 <<http://www.ft.com/cms/s/0/63e82206-dff8-11e3-b709-00144feabdc0.html#ixzz396lpPeAA>>.

⁷⁷ Philip Stafford, ‘Qatar to Sell Down Stake in LSE’, *Financial Times* (online), 9 July 2014 <<http://www.ft.com/cms/s/0/91db6bd2-07a3-11e4-8e62-00144feab7de.html#ixzz396nZNCtt>>.

⁷⁸ ASX-SGX, ‘ASX and SGX Combine to Create the Premier International Exchange in Asia Pacific – The Heart of Global Growth’ (Joint News Release, 25 October 2010) <http://www.asx.com.au/resources/newsletters/listed_at_asx/20101201_asx_sgx_merger_proposal.htm>.

⁷⁹ Reuters, ‘How the ASX-SGX Merger Failed’, *The Sydney Morning Herald* (online), 21 April 2011 <<http://www.smh.com.au/business/how-the-asxsgx-merger-failed-20110421-1dqb2.html>>.

- 1 November 2010** ACCC commences review under the Merger Review Process Guidelines.⁸⁰
- 15 December 2010** After reviewing submissions from interested parties,⁸¹ the ACCC announces it will not oppose the proposed acquisition.⁸²
- 8 April 2011** On advice from the Foreign Investment Review Board, the then Treasurer of Australia Wayne Swan refuses to grant permission for the merger as it is not in the best interests of Australia. SGX walks away from the merger deal after the rejection by the Treasurer.⁸³
- 20 May 2014** ASX and SGX announce cooperation to further enhance market connectivity where a range of international products and services will be available to Australian customers.⁸⁴

F.4 Toronto Stock Exchange and London Stock Exchange/Maple

- 9 February 2011** London Stock Exchange Group plc (LSEG) and TMX Group (TMX) announce an agreement for a merger of equals. The plan aims to pool global capital and expertise from both entities and to create a more diversified business for shareholders across both groups. The merged group has more than 6,700 companies listed with a market capitalisation of about £3.7 trillion.⁸⁵ The group will become the largest exchange by the number of listed companies and for natural resources, mining, energy and clean technology companies, if the merger succeeds.⁸⁶
- 13 June 2011** Maple Group Acquisition Corporation (Maple), formed by nine Canadian pension funds and banks, initiates a hostile takeover in hoping to block the TMX from taking over by LSEG. The rival bid is a combination of stock and cash of CAD \$3.7 billion.
- 22 June 2011** The LSEG and TMX agree to pay a special dividend to shareholders to counter the Maple bid and to persuade shareholders to vote for the LSEG's offer.

⁸⁰ ACCC, *Singapore Exchange Limited – Proposed Acquisition of ASX Limited* (15 December 2010) <<http://registers.accc.gov.au/content/index.phtml/itemId/962036>>.

⁸¹ Ibid.

⁸² Ibid.

⁸³ Eric Johnston, 'Singapore Finally Walks from ASX Bid', *The Sydney Morning Herald* (online), 8 April 2011 <<http://www.smh.com.au/business/singapore-finally-walks-from-asx-bid-20110408-1d6o4.html>>.

⁸⁴ Australian Stock Exchange, 'ASX and SGX Cooperate to Further Enhance Market Connectivity' (Media Release, 20 May 2014) <http://www.asx.com.au/documents/asx-news/ASX_and_SGX_Further_Enhance_Connectivity.pdf>.

⁸⁵ 'LSE Agrees Merger with TMX of Canada', *BBC* (online), 9 February 2011 <<http://www.bbc.com/news/business-12400785>>.

⁸⁶ London Stock Exchange Group, 'London Stock Exchange Group Plc and TMX Group Inc Join Forces in Merger of Equals' (Press Release, 9 February 2011) <<http://www.lseg.com/media-centre/news/corporate-press-releases/london-stock-exchange-group-plc-and-tmx-group-inc-join-forces-merger-equals>>.

29 June 2011	The deal to merge is terminated by both parties due to a lack of shareholder support. On the termination of the agreement, the TMX Group pays LSEG C\$10 million as expense fee and a further C\$29 million is paid to LSEG if TMX enters a definitive agreement with Maple. ⁸⁷
4 July 2012	The Ontario Securities Commission (OSC) approves the takeover of TMX by Maple, subject to certain conditions.
31 July 2012	The Maple Group wins control of the TMX Group Inc with 91% of TMX shares tendered. The offer is C\$50 in cash per share tendered. ⁸⁸ The Maple Group Acquisition Corporation is renamed TMX Group Limited. ⁸⁹
12 September 2012	TMX Group Inc's shareholders approve an Arrangement of TMX Group limited to acquire all outstanding shares of TMX Group Inc and becomes fully owned by TMX Group Inc. ⁹⁰
13 September 2012	The Ontario Superior Court of Justice issues a final order approving the Arrangement. ⁹¹
14 September 2012	The TMX Group Limited announces that it has completed its takeover of TMX Group Inc. The Group after the merger will control 85% of equities in Canada. ⁹²

F.5 Hong Kong Stock Exchange and Shanghai Stock Exchange

March 2000	Mergers of The Stock Exchange of Hong Kong Limited (SEHK), Hong Kong Futures Exchange Limited (HKFE) and Hong Kong Securities Clearing Company Limited (HKSCC) to form Hong Kong Exchanges and Clearing Limited (HKEx). ⁹³

⁸⁷ London Stock Exchange Group, 'Announcement Re LSEG/TMX Group Merger' (Press Release, 29 June 2011) <<http://www.lseg.com/media-centre/news/corporate-press-releases/announcement-re-lsegtmx-group-merger>>.

⁸⁸ Sunny Freeman, 'Maple Group Wins Control of TMX, with 91 Percent of Shares Tendered', *The Global and Mail* (online), 31 July 2012 <<http://www.theglobeandmail.com/report-on-business/maple-group-wins-control-of-tmx-with-91-per-cent-of-shares-tendered/article4453456/>>.

⁸⁹ CIBC Mellon, *Maple-TMX Acquisition Completed: Maple (now "TMX Group Ltd") Shares Begin Trading Sept 19* (19 February 2012) <https://www.cibcmellon.com/Contents/en_CA/English/NewsRoom/BulletinsReleases/2012/NB20120917.html>.

⁹⁰ Ibid.

⁹¹ Ibid.

⁹² Richard Warnica, 'Maple Completes TMX Takeover, Watchdogs on Alert', *Canadian Business* (online), 12 September 2012 <<http://webcache.googleusercontent.com/search?q=cache:Xb3LAPkrI3MJ:www.canadianbusiness.com/investing/maple-completes-tmx-takeover-watchdogs-on-alert/+&cd=2&hl=en&ct=clnk&gl=au>>.

⁹³ Hong Kong Exchanges and Clearing Limited, *History of HKEx and its Markets* (31 October 2013) <<https://www.hkex.com.hk/eng/exchange/corpinfo/history/documents/hkex-01e.pdf>>.

June 2000	HKEx lists itself on SEHK by introduction ⁹⁴
June 2003	Signing of the Closer Economic Partnership Arrangement (CEPA) between Hong Kong and Mainland ⁹⁵
November 2003	After CEPA, HKEx opens its first representative office in Beijing ⁹⁶
October 2005	The third phase of Closer Economic Partnership Arrangement (CEPA III) is signed. Qualified Mainland securities and futures companies are permitted to establish branches in Hong Kong. ⁹⁷
January 2009	HKEx signs a Closer Cooperation Agreement (CCA) with the Shanghai Stock Exchange (SSE). The CCA aims to contribute to the greater development of China's economy, meeting the domestic and international fund-raising needs of Chinese enterprises. ⁹⁸
April 2009	HKEx signs a CCA with the Shenzhen Stock Exchange (SZSE).
October 2011	BRICS exchanges alliance is announced. The alliance includes BM&FBOVESPA, MICEX from Russia, Hong Kong Exchanges and Clearing Limited (HKEx) and Johannesburg Stock Exchange (JSE) from South Africa. The alliance allows all exchanges to cross list benchmark equity index derivatives on the boards of each of the other alliance members. ⁹⁹
December 2012	HKEx outbids ICE and acquires the London Metal Exchange for US \$2.16 billion ¹⁰⁰
2 April 2014	The HKEx announces the potential establishment of mutual market connectivity initiatives allowing mutual stock market access between Mainland China and Hong Kong. ¹⁰¹
17 November 2014	The Shanghai-Hong Kong Stock Connect is launched. ¹⁰²

⁹⁴ Ibid

⁹⁵ Ibid

⁹⁶ Ibid

⁹⁷ Ibid

⁹⁸ Ibid

⁹⁹ BM&FBOVESPA, 'BRICS Exchanges Alliance Announced' (News Release, 13 October 2013) <<http://www.bmfbovespa.com.br/en-us/News/2011/BRICS-exchanges-alliance-announced-2011-10-13.aspx?tipoNoticia=1&idioma=en-us>>; Hong Kong Exchanges and Clearing Limited, *BRICS*mart <<https://www.hkex.com.hk/eng/prod/drprod/brics/Documents/bricsmart.pdf>>.

¹⁰⁰ London Metal Exchange, 'HKEx and LME Announce Completion of Transaction' (Press Release, 6 December 2012) <<http://www.lme.com/en-gb/news-and-events/press-releases/press-releases/2012/12/hkex-and-lme-announce-completion-of-transaction/>>.

¹⁰¹ Hong Kong Exchanges and Clearing Limited, 'Proposed Establishment of Mutual Market Access and Resumption of Trading' (News Release, 10 April 2014) <<http://www.hkex.com.hk/eng/newsconsul/hkexnews/2014/Documents/1404102news.pdf>>.

¹⁰² Gregor Stuart Hunter, 'Shanghai-Hong Kong Trading Has a Slow First Month', *The Wall Street Journal* (online), 16 December 2014 <<http://www.wsj.com/articles/china-shanghai-hong-kong-stock-connect-program-has-tepid-first-month-1418729854>>.

F.6 NASDAQ

11 March 1998	American Stock Exchange (Amex) enters into merger discussions with Nasdaq. ¹⁰³
19 March 1998	The boards of Amex and National Association of Securities (NASD) approve a preliminary agreement for the merger. ¹⁰⁴
8 April 1998	The board of Amex approves an agreement to merge with the NASD. ¹⁰⁵
10 April 1998	The board of NASD approves an agreement to acquire Amex. ¹⁰⁶
25 June 1998	Amex seatholders approve merger with Nasdaq. ¹⁰⁷
30 October 1998	SEC approves the deal between Amex and Nasdaq. ¹⁰⁸
2 November 1998	NASD completes the merger with Amex. ¹⁰⁹
15 April 2000	Members of NASD vote for a private placement spin off of Nasdaq. Nasdaq later gains independence from NASD and, through issuing privately placed stock, it becomes a for-profit shareholder-owned market. ¹¹⁰
15 march 2001	Nasdaq submits an initial application for exchange status. ¹¹¹
10 February 2005	Nasdaq's common stock is listed on the Nasdaq Stock Market. ¹¹²
13 January 2006	Nasdaq receives approval from SEC to become a registered national securities exchange ¹¹³ . This status is important for Nasdaq because traditionally Nasdaq is part of NASD which acts as a regulatory body for Nasdaq. Since Nasdaq is going to be independent, the SEC must be

¹⁰³ 'Report: Nasdaq, Amex Exchanges Discussing Merger', *AP Online* (online), 12 March 1998 <<http://www.highbeam.com/doc/1P1-19805735.html>>.

¹⁰⁴ Sharon Walsh, 'NASD, Amex Vote to Combine Markets: Regional Venues Could Join Alliance', *The Washington Post* (online), 19 March 1998 <<http://www.highbeam.com/doc/1P2-643847.html>>; Deborah Lohse, 'NASD, Amex Boards Approve Agreement to Merge Markets', *The Wall Street Journal* (online), 19 March 1998 <<http://www.wsj.com/articles/SB890243463309222500>>.

¹⁰⁵ 'Amex Board Approves Plan to Merge with Nasdaq Stock Market', *Dow Jones* (online), 8 April 1998 <<https://global.factiva.com/>>.

¹⁰⁶ 'Nasdaq Approves Amex Buy', *New York Post* (online), 10 April 1998 <<https://global.factiva.com/>>.

¹⁰⁷ Andrew Fraser, 'Amex Seat Holders Approve Merger with Nasdaq', *Associated Press Newswires* (online), 25 June 1998 <<http://www.highbeam.com/doc/1P2-16771137.html>>.

¹⁰⁸ Amy Feldman, 'SEC Seen Giving Okay to NASDAQ/AMEX Deal', *New York Daily News* (online), 30 October 1998 <<http://www.nydailynews.com/archives/money/sec-giving-nasdaq-amex-deal-article-1.812266>>.

¹⁰⁹ 'Amex-Nasdaq Complete Merger That Creates "Market of Markets"', *Associated Press Newswires* (online), 2 November 1998 <<https://global.factiva.com/>>.

¹¹⁰ Congressional Record S21193 (Gary Shorter) (daily ed, 29 March 2005) <<http://congressionalresearch.com/RS21193/document.php?study=Nasdaq+Pursuit+of+Exchange+Status+and+an+Initial+Public+Offering>>.

¹¹¹ Ibid.

¹¹² SEC, *Form 10-K – Annual Report for the fiscal year ended December 31 2014*, p 27, pt II, item 5.

¹¹³ Ibid.

satisfied with the regulatory oversight of this new independent body before the link between NASD and Nasdaq can be severed.

- 10 March 2006** Nasdaq offers 2.4 billion pounds (USD \$4.2 billion) to take over LSE.¹¹⁴ The aim of the merger is to create a single trans-Atlantic marketplace to trade both US and European listed stocks simultaneously in US and London on any business day.¹¹⁵
- 13 March 2006** LSE rejects the Nasdaq takeover. LSE argues that the offer does not reflect the true value of the exchange.¹¹⁶
- 6 April 2006** Rumours indicate the possibility of Nasdaq taking over Singapore Stock Exchange.¹¹⁷
- 8 April 2006** SGX explicitly denies it is in merger talks with the Nasdaq exchange.¹¹⁸
- 11 September 2006** Nasdaq is in early talks with Nordic stock exchange operator OMX AB.¹¹⁹ Shares of OMX AB rises 5.7 percent after the news.
- 8 October 2006** LSE's strong growth in the half yearly result suggests that the offer by Nasdaq should be higher than 2.7 billion pounds.¹²⁰
- 20 November 2006** Nasdaq initiates a hostile takeover on LSE. The offer increases 20.8 percent in value compared to the offer in March. The deal is now worth 2.9 billion pounds.¹²¹ The bid is rejected unanimously by the LSE's board within hours.¹²²
- May 2007** Nasdaq announces its offer to each OMX AB shareholder of 0.502 new Nasdaq share plus 94.3 SEK in cash.¹²³ The deal is worth \$3.7 billion USD.¹²⁴
- 3 October 2007** Nasdaq agrees to acquire the Boston Stock Exchange for \$61 million

¹¹⁴ Jane Wardell, 'LSE Gets, Nixes Nasdaq Takeover Approach', *Associated Press Newswires* (online), 10 March 2006 <<https://global.factiva.com/>>.

¹¹⁵ Ibid.

¹¹⁶ Ibid.

¹¹⁷ Uma Shankari, 'Talk of Nasdaq Takeover Propels SGX', *Business Times Singapore* (online), 7 April 2006 <<https://global.factiva.com/>>.

¹¹⁸ Goh Eng Yeow, 'SGX Slides Following Denial of Nasdaq Takeover Talks', *Straits Times* (online), 8 April 2006 <<https://global.factiva.com/>>.

¹¹⁹ 'Shares in Nordic Stock Exchange Operator Surge amid Reports of Nasdaq Takeover Plans', *Associated Press Newswires* (online), 11 September 2006 <<https://global.factiva.com/>>; Louise Nordstrom, 'OMX Soars on Reports of Nasdaq Takeover', *Dow Jones International News* (online), 11 September 2006 <<https://global.factiva.com/>>.

¹²⁰ Jill Treanor, 'LSE Fends Off Nasdaq Takeover Threat with Strong Growth and Pounds 2.7bn Price Tag', *The Guardian* (online), 9 November 2006 <<https://global.factiva.com/>>.

¹²¹ 'Nasdaq Takeover Offer for LSE Turns Hostile', *Agence France Presse* (online), 20 November 2006 <<https://global.factiva.com/>>.

¹²² John Revill, 'LSE Rejects £2.7 bn Nasdaq Takeover', *Birmingham Post* (online), 21 November 2006 <<https://global.factiva.com/>>.

¹²³ 'Stockwatch OMX Shares Surge on Nasdaq Takeover Offer: Analysts Broadly Positive', *AFX Asia* (online), 25 May 2007 <<https://global.factiva.com/>>.

¹²⁴ 'News Highlights: Top Equities Stories of the Day', *Dow Jones International News*, 25 May 2007.

	USD. ¹²⁵
8 November 2007	Nasdaq agrees to buy the Philadelphia Stock Exchange for \$652 million USD. ¹²⁶
26 December 2007	Nasdaq obtains antitrust clearance from the Federal Trade Commission to purchase the Philadelphia Stock Exchange. ¹²⁷
3 January 2008	The board of directors of OMX AB recommends shareholders to accept the takeover offer from Nasdaq. ¹²⁸
25 January 2008	The Financial Markets Advisory Committee advises the Swedish Government to approve the takeover of OMX AB by Nasdaq. ¹²⁹
27 February 2008	Nasdaq OMX Group Inc is formed. ¹³⁰
24 July 2008	Nasdaq completes acquisition of the Philadelphia Stock Exchange. ¹³¹
29 August 2008	Nasdaq completes acquisition of the Boston Stock Exchange ¹³²
19 November 2009	Swedbank agrees to sell its 13.2 percent stake of Tallinn Exchange to give Nasdaq OMX full ownership of the exchange. ¹³³
24 March 2010	Nasdaq OMX concludes acquisition of outstanding shares of Tallinn Exchange. ¹³⁴
17 February 2011	Following the announcement of potential merger worth \$9 billion between Deutsche Boerse AG and NYSE Euronext, Nasdaq OMX and IntercontinentalExchange Inc are looking to rival the Deutsche bid to NYSE Euronext. ¹³⁵

¹²⁵ 'Deals & Dealmakers: Nasdaq to Buy Boston Stock Exchange', *The Wall Street Journal* (online), 3 October 2007 <<https://global.factiva.com/>>.

¹²⁶ Tulsa World, 'Nasdaq Purchasing Philadelphia Stock Exchange', *Bloomberg AP and Staff Reports* (online), 8 November 2007 <<https://global.factiva.com/>>.

¹²⁷ 'DJ Nasdaq Gets Antitrust OK to Buy Philadelphia Stock Exchange', *Dow Jones Chinese Financial Wire* (online), 26 December 2007 <<https://global.factiva.com/>>.

¹²⁸ 'NDAQ Globe/wire Say OMX Board Gives Nasdaq Takeover the Nod', *Canada Stockwatch* (online), 3 January 2008 <<https://global.factiva.com/>>.

¹²⁹ 'Government Committee Says Sweden's OMX Would Profit from Nasdaq Takeover', *Associated Press Newswires* (online), 25 January 2008 <<https://global.factiva.com/>>.

¹³⁰ Nasdaq, *Nasdaq OMX Group Inc (NDAQ): New Analyst Report from Zacks Equity Research - Zacks Equity Research Report* (5 December 2013) <<http://www.nasdaq.com/article/nasdaq-omx-group-inc-ndaq-new-analyst-report-from-zacks-equity-research-zacks-equity-research-report-cm309331#ixzz3XtYEt0XM>>.

¹³¹ 'NASDAQ OMX Group to Complete Acquisition of the Philadelphia Stock Exchange: NASDAQ OMX to Broaden Its Entry into Derivatives Market', *PrimeNewswire* (online), 24 July 2008 <<https://global.factiva.com/>>.

¹³² 'NDAQ NASDAQ Completes Acquisition of Boston Stock Exchange', *Canada Stockwatch* (online), 29 August 2008 <<https://global.factiva.com/>>.

¹³³ 'Swedbank Sells Shares in Tallinn Exchange to NASDAQ OMX to Improve Ability to Develop More Liquid Baltic Capital Markets', *ENP Newswire* (online), 19 November 2009 <<https://global.factiva.com/>>.

¹³⁴ 'NASDAQ OMX Concludes Acquisition of Outstanding Shares', *RIA Oreanda-News* (online), 24 March 2010.

¹³⁵ 'Nasdaq, ICE in "Critical Stage" Talks – Report', *Reuters News*, 17 February 2011 <<https://global.factiva.com/>>.

1 April 2011	Nasdaq and ICE offer to buy NYSE Euronext for \$42.50 in cash and stock per share, with a total value of \$11.3 billion. ¹³⁶
8 April 2011	NYSE rejects Nasdaq-ICE bid as NYSE believes the bid is a strategic mistake and is not in the best interests of NYSE's shareholders. ¹³⁷
17 May 2011	Nasdaq-ICE drops their \$11 billion bid after the Department of Justice's antitrust division threatens to block the deal. ¹³⁸

F.7 OMX Background Timeline

Before the acquisition by Nasdaq in 2007, the OMX Group has eight stock exchanges across the Nordic and Baltic regions. These include Copenhagen Stock Exchange, Stockholm Stock Exchange, Helsinki Stock Exchange, Tallinn Stock Exchange, Riga Stock Exchange, Vilnius Stock Exchange, Iceland Stock Exchange and Armenian Stock Exchange.

30 June 1999	OM acquires the Stockholm Stock Exchange. It will be renamed as OM Stockholm Exchange. ¹³⁹
12 August 2002	HEX (Helsinki Stock Exchange) Group acquires Riga Stock Exchange. ¹⁴⁰
July 2003	OM and LSE co-develop and operate the EDX derivatives exchange. ¹⁴¹
6 October 2003	OM and HEX Group merge to become OMHEX. ¹⁴²
31 August 2004	OMHEX changes its name to OMX AB and is structured into two divisions – the operation of the Nordic and Baltic stock markets and OMX technology. ¹⁴³

¹³⁶ '5th Update: Nasdaq, ICE Offer to Buy NYSE Euronext for \$11.3 Billion', *Dow Jones Business News* (online), 1 April 2011 <<https://global.factiva.com/>>.

¹³⁷ 'NYSE Rejects Nasdaq-ICE Bid as "Strategic Mistake"', *FOI* (online), 8 April 2011 <<https://global.factiva.com/>>.

¹³⁸ Jacob Bunge and William Launder, 'Nasdaq, ICE Pull Bid for NYSE', *The Wall Street Journal Europe* (online), 17 May 2011 <<https://global.factiva.com/>>.

¹³⁹ 'Stockholm Stk Exchange to Become OM Stockholm Exchange', *Dow Jones International News* (online), 30 June 1999 <<https://global.factiva.com/>>.

¹⁴⁰ 'Helsinki Stock Exchange Completes Purchase of Riga Bourse', *Agence France-Presse* (online), 12 August 2002 <<https://global.factiva.com/>>.

¹⁴¹ 'Liffe to Challenge LSE's EDX Exchange', *eFinancial News* (online), 25 September 2003 <<https://global.factiva.com/>>.

¹⁴² 'OMHEX Owns All Shares in HEX', *PrimeZone Media Network* (online), 6 October 2003 <<https://global.factiva.com/>>.

¹⁴³ 'OMHEX Changes Name to OMX', *PrimeZone Media Network* (online), 31 August 2004 <<https://global.factiva.com/>>.

January 2005	OMX and Copenhagen Stock Exchange merge at a value of 1.22 billion Danish krone. ¹⁴⁴
September 2006	OMX and the Iceland Stock Exchange merge at a value of 250 million SEK. ¹⁴⁵
21 November 2007	OMX signs a formal deal with the Government of Armenia to acquire the Armenian Stock Exchange. ¹⁴⁶
August 2007	OMX is acquired by Nasdaq. ¹⁴⁷

¹⁴⁴ Brenda Goh and Louise Heavans, 'Factbox: A History of Global Exchange Merger Activity', *Reuters* (online), 16 May 2011 <<http://www.reuters.com/article/2011/05/16/us-factbox-exchanges-idUSTRE74F4RJ20110516>>.

¹⁴⁵ Ibid.

¹⁴⁶ 'OMX Acquires the Armenian Stock Exchange and the Central Depository of Armenia', *Cision* (online), 21 November 2007 <<http://news.cision.com/omx/r/omx-acquires-the-armenian-stock-exchange-and-the-central-depository-of-armenia,c314721>>.

¹⁴⁷ 'NASDAQ OMX Concludes Acquisition of Outstanding Shares', above n 134.

Part G Case Studies

G.1 London Stock Exchange

I ORIGINS

London already had a market for share trading during the 18th century which had ‘provide[d] funding for the many voyages of discovery, overseas trading, and foreign military campaigns’.¹ In 1698, ‘[s]tock dealers [were] expelled from the Royal Exchange for rowdiness’ and began meeting at ‘Jonathan’s Coffee House’ instead.² In 1761, 150 brokers formed a club at this venue and constructed their own premises in 1773, which they soon renamed “The Stock Exchange.”³ In 1801, ‘the business reopens under a formal membership subscription basis.’⁴

The Industrial Revolution saw infrastructure projects emerge and ‘provided the basis for the modern period of shareholder-based corporations.’⁵ Another twenty stock exchanges appeared in the United Kingdom over the course of the 19th century.⁶ Developments during this period included the London Stock Exchange’s introduction of the ticker tape in 1872, an invention which ‘in turn enabled trades to take place elsewhere than the market floor.’⁷ A new Deed of Settlement was entered in 1875 and became effective from 1876⁸ meant that the exchange ‘began operating on behalf of its owner-members instead of just its members,’⁹ however, ‘[m]embers remained responsible for the company’s debts and operational obligations.’¹⁰ The Association of Stock Exchanges was formed in 1890 between the various stock exchanges in the United Kingdom.¹¹

II PERIODS OF SUSPENSION

Trade was suspended on the Stock Exchange from July 1914 until 1915, though its usual operations did not recommence until 1918.¹² In 1939, due to imminent impact of the World War Two, the Exchange was closed for 6 days.¹³ In 1945, the floor of the House was damaged by a V2 rocket and the Exchange was closed for one day.¹⁴ Trading then continued in the basement after.¹⁵

¹ ‘London Stock Exchange Group plc’ in and Tina Grant (ed), *International Directory of Company Histories, Volume 156* (St James Press, 2014) 246, 246.

² London Stock Exchange, *Our History* (7 July 2015) <<http://www.londonstockexchange.com/about-the-exchange/company-overview/our-history/our-history.htm>>.

³ Ibid.

⁴ Ibid.

⁵ ‘London Stock Exchange Group plc’, above n 1.

⁶ Ibid.

⁷ Ibid.

⁸ Ibid; London Stock Exchange, *Our History*, above n 2.

⁹ ‘London Stock Exchange Group plc’, above n 1.

¹⁰ Ibid.

¹¹ Ibid.

¹² Ibid 246-47.

¹³ London Stock Exchange, *Our History*, above n 2.

¹⁴ Ibid.

¹⁵ Ibid.

III DEMUTUALISATION AND LISTING

Consolidation of the various exchanges into the LSE began in 1973.¹⁶ The LSE ‘became a private limited company (plc) with its member broker firms becoming shareholders’¹⁷ following legislative changes under the Companies Act of 1985.¹⁸ However, shareholders did not receive profits, which were ‘returned to the company for infrastructure and other development costs.’¹⁹

A number of developments occurred on October 27, 1986, effected by the Prime Minister of the United Kingdom at the time, Margaret Thatcher, which have become known as the “Big Bang”.²⁰ The rules of the LSE have changed significantly and dramatically open up the financial market in London. The LSE was converted to a private limited company under the *Companies Act 1985*. The measures effected included allowing member firms to be owned by outside corporation, permitting firms to have dual roles as brokers and dealers, abolishing minimum scales of commission, stripping voting rights from individual members and changing trading from open-outcry to electronic via computer and telephone.²¹

In 1991, the Exchange adopted a new trading name ‘The London Stock Exchange’.²²

In 1995, the Alternative Investment Market was ‘created specifically for startups and smaller companies’²³ such as had proved popular with NASDAQ in the US.²⁴ In 1997, LSE’s own Stock Exchange Electronic Trading Service (SETS) and CREST settlement service were introduced.²⁵

In 2000, the LSE handed over its role as ‘UK Listing Authority with HM Treasury’ to the Financial Services Authority (FSA). In the same year, shareholders have voted for the Exchange to become a public limited company – the London Stock Exchange plc.²⁶ In 2000, the year commemorating the 200th anniversary of the LSE, the Exchange was listed on its Main Market in July.²⁷

IV A SERIES OF TAKEOVER AND MERGER ATTEMPTS

The LSE proposed a merger with the Frankfurt Stock Exchange, although this idea was discarded later on.²⁸ The Swedish stock exchange OM Gruppen failed in a hostile takeover bid of the LSE at the same time.²⁹ NASDAQ attempted a similar acquisition in 2007, which

¹⁶ ‘London Stock Exchange Group plc’, above n 1, 247.

¹⁷ Ibid.

¹⁸ Ibid.

¹⁹ Ibid.

²⁰ Ibid 247-248.

²¹ London Stock Exchange, *Our History*, above n 2.

²² Ibid.

²³ ‘London Stock Exchange Group plc’, above n 1, 248.

²⁴ Ibid.

²⁵ ‘London Stock Exchange Group plc’, above n 1, 248.

²⁶ Ibid

²⁷ London Stock Exchange, *Our History*, above n 2.

²⁸ ‘London Stock Exchange Group plc’, above n 1, 248-249.

²⁹ Ibid 249.

was also the year when the LSE acquired the Borsa Italiana.³⁰ The LSE was unsuccessful in its attempt at a merger with TMX in 2011.³¹

G.2 Euronext N.V. and NYSE

I NYSE ORIGINS

The New York Stock Exchange began as a group of merchants and brokers meeting in the Tontine Coffee House on the corner of Wall and Water Streets in the 1790s.³² In 1792, 24 brokers signed the “Buttonwood Agreement” which set up the Exchange.³³ ‘They agreed to avoid public auctions, to collect minimum commissions on federal bonds (public stock), and to “give preference to each other” in their trading deals.’³⁴

In 1817, the New York Stock & Exchange Board was created,³⁵ ‘with a fixed location and regular hours.’³⁶ Many federal securities were traded in the following decades, ‘financ[ing] the construction of roads, bridges, canals, and municipal water, sewerage, and lighting systems.’³⁷ There was an economic downturn from the 1830s, but ‘the NYS&EB managed to survive until the down cycle reversed in 1843.’³⁸ Railroad shares were heavily traded by the 1850s and 60s.³⁹ It was renamed the New York Stock Exchange in 1863,⁴⁰ and moved into a new, permanent location in 1865.⁴¹ ‘With the end of the Civil War, intense capitalization of American industry spurred unprecedented growth in stock trading and the emergence of new and competing exchanges.’⁴² The volume of trading increased over this time and continuous trading was soon introduced.⁴³

II DEVELOPMENTS AND PERIODS OF SUSPENSION

Major technological developments also occurred during the century, with the introduction of the telegraph and ‘the telephone, which reduced trading time from roughly 15 minutes to less than sixty seconds after 1878’.⁴⁴ Gold speculation causes Black Friday on September 24, 1869.⁴⁵ ‘In September 1873, the failure of Jay Cooke & Company sparked another major

³⁰ Ibid.

³¹ Ibid.

³² ‘New York Stock Exchange, Inc’ in Tina Grant (ed), *International Directory of Company Histories, Volume 39* (St James Press, 2001), 296.

³³ Ibid; NYSE, *Timeline* (2014) <http://www1.nyse.com/about/history/timeline_events.html>.

³⁴ ‘New York Stock Exchange, Inc’, above n 32, 296.

³⁵ Ibid; NYSE, *Timeline*, above n 33.

³⁶ ‘New York Stock Exchange, Inc’, above n 32, 296.

³⁷ Ibid.

³⁸ Ibid.

³⁹ Ibid 297.

⁴⁰ Ibid; NYSE, *Timeline*, above n 33.

⁴¹ NYSE, *Timeline*, above n 33.

⁴² ‘New York Stock Exchange, Inc’, above n 32, 297.

⁴³ Ibid.

⁴⁴ Ibid.

⁴⁵ Ibid; NYSE, *Timeline*, above n 33.

market break that closed NYSE offices for ten days and scared the securities industry until the end of the decade'.⁴⁶ The NYSE then moved location in 1903 to 18 Broad Street.⁴⁷

III OTHER SIGNIFICANT EVENTS AND DEVELOPMENTS

Disruptions to trading include 'The Panic of 1907', the beginning of World War I in 1914, and Black Thursday on 24 October 1929.⁴⁸

'The United States Congress passed corrective legislation, of which the Securities Act of 1933 and the Securities Exchange Act of 1934 directly influenced the NYSE. The 1933 Act mandated the registration of all new issues of securities with the Federal Trade Commission (FTC) and the full availability of all pertinent information to investors. The later Act created the Securities and Exchange Commission (SEC) to monitor price manipulation, speculation, and unfair practices in all securities exchanges. On October 1, 1934, the NYSE registered with the SEC as a national securities exchange.'⁴⁹

On November 22, 1963, an early closure of the Exchange to avoid panic selling of stocks was warranted after the President Kennedy of the United States was assassinated.⁵⁰ In 1971, 'the NYSE was incorporated as a not-for profit organization.'⁵¹ On October 19, 1987, Black Monday occurs.⁵² During the 1990s, the NYSE faced competition from other trading systems, particularly NASDAQ.⁵³ On September 11, 2001, when terrorist attacks destroyed the World Trade Center in New York, the NYSE was close for four days -- its longest closure since 1933. On the day of its reopening on September 17, it set a record volume of 2.37 billion shares.⁵⁴

IV NYSE MERGES WITH ARCAEX

In 2006, a merger between NYSE and ArcaEx results in the formation of the 'for-profit, publicly-owned company'⁵⁵ NYSE Group, Inc.⁵⁶ At this time, the NYSE remained 'a floor-based auction stock market',⁵⁷ though there was also an option for electronic trading, and an increased use of electronic trading technologies.⁵⁸ NYSE Arca, which was formed through the merger, operated alongside the NYSE, and was described as 'the first open, all-electronic stock market in the United States for trading equity securities listed on NYSE Arca, the

⁴⁶ 'New York Stock Exchange, Inc', above n 32, 297.

⁴⁷ NYSE, *Timeline*, above n 33; 'New York Stock Exchange, Inc', above n 32, 297, 298 (Key Dates).

⁴⁸ 'New York Stock Exchange, Inc', above n 32, 297. *Timeline*.

⁴⁹ *Ibid* 297-298.

⁵⁰ NYSE, *Timeline*, above n 33.

⁵¹ 'New York Stock Exchange, Inc', above n 32, 298; NYSE, *Timeline*, above n 33.

⁵² *Ibid*.

⁵³ 'New York Stock Exchange, Inc', above n 32, 297.

⁵⁴ NYSE, *Timeline*, above n 33.

⁵⁵ *Ibid*.

⁵⁶ *Ibid*.

⁵⁷ NYSE Group, Inc, *Form 10-K Annual Report* (Company Report, 31 December 2005), 6.

⁵⁸ *Ibid*.

NYSE, Nasdaq and AMEX, as well as ETFs and other exchange-listed securities.⁵⁹ Equity options could be traded as well.⁶⁰

V EURONEXT N.V. ORIGINS

Euronext NV (Euronext) is the result of a merger in 2000 of the Amsterdam Stock Exchange⁶¹ the Paris Bourse⁶² and the Brussels Stock Exchange.⁶³

Additionally, in 2002 Euronext expanded further by acquiring the London International Financial Futures and Options Exchange (LIFFE),⁶⁴ and merging with Bolsa de Valores de Lisboa e Porto (BVLPP), a Portuguese Exchange.⁶⁵

VI NYSE MERGED WITH EURONEXT N.V.

On June 1, 2006, Euronext and NYSE entered into an agreement for a merger of equals.⁶⁶ This merger was of significance in terms of its scale as the first involving consolidation of transatlantic exchanges. A new entity, NYSE Euronext, was formed on April 4, 2007, after securing shareholders' approval from the two entities and regulatory approvals from all relevant authorities.⁶⁷

Not long after the transatlantic merger, on October 1, 2008, NYSE Euronext merged with the American Stock Exchange (Amex).⁶⁸

During its five years of life, NYSE Euronext was subjected to a number of bids and offers from other exchanges. In 2011, Deutsche Boerse fought with NASDAQ OMX and ICE to gain control of NYSE Euronext, despite the fact that both of the deals failed through on anti-trust grounds.⁶⁹

⁵⁹ Ibid 18.

⁶⁰ Ibid 18.

⁶¹ NYSE Euronext, *Amsterdam Stock Exchange* (2013) <<http://www.nyx.com/who-we-are/history/amsterdam>>.

⁶² NYSE Euronext, *Paris: It Started with the Lyons Bourse* (2013) <<http://www.nyx.com/who-we-are/history/paris>>.

⁶³ NYSE Euronext, *Brussels Stock Exchange* (2013) <<http://www.nyx.com/who-we-are/history/brussels>>.

⁶⁴ NYSE Euronext, *London: The LIFFE* (2013) <<http://www.nyx.com/who-we-are/history/london>>.

⁶⁵ Ibid.

⁶⁶ NYSE, 'NYSE Group and Euronext Announce Merger' (News Briefs, June 2006) <<http://www1.nyse.com/about/publication/1145959806931.html>>.

⁶⁷ NYSE, *Timeline*, above n 33; Aaron Lucchetti and Alistair MacDonald, 'Euronext Holders Approve Deal for Historic Merger with NYSE', *The Wall Street Journal* (online) <<http://www.wsj.com/articles/SB116653086274154451>>; NYSE, 'NYSE Group Shareholders Overwhelmingly Approve Combination with Euronext, Preliminary Results Indicate — Approximately 99.7 Percent of Voting Shareholders in Favor of Merger' (News Release, 20 December 2006) <<http://www1.nyse.com/press/1166613560168.html>>.

⁶⁸ NYSE, 'NYSE Euronext Completes Acquisition of American Stock Exchange' (News Release, 1 October 2008) <<http://www1.nyse.com/press/1222772889985.html>>.

⁶⁹ NYSE, 'Deutsche Boerse AG And NYSE Euronext Agree To Combine To Create The Premier Global Exchange Group' (News Release, 15 February 2011) <<http://www1.nyse.com/press/1297768048707.html>>; Ken Sweet, 'NYSE, Deutsche Boerse Agree to Merge', *CNN Money* (online), 15 February 2011 <http://money.cnn.com/2011/02/15/markets/NYSE_exchange_merger/index.htm?iid=EL>; Ben Rooney, 'NYSE Shuns Second Offer from Nasdaq and ICE', *CNN Money* (online), 21 April 2011 <http://money.cnn.com/2011/04/21/news/companies/nyse_rejects_nasdaq_ice_again/index.htm?iid=EL>; Aaron Smith, 'Nasdaq and ICE Withdraw NYSE bid', *CNN Money* (online), 16 May 2011; Aaron Smith, Catherine Tymkiw and Mark M Meinero, 'NYSE-Frankfurt Stock Exchange Merger Blocked', *CNN Money* (online), 1 February 2012

G.3 Intercontinental Exchange Inc. and the new Euronext N.V.

I ORIGINS AND MAJOR DEVELOPMENTS

The development of Intercontinental Exchange Inc began in 1997 when Jeffrey Sprecher ‘simply acquired a controlling interest in Continental Power,’⁷⁰ a company then based in Atlanta. Continental Power had been ‘a small technology outfit that used a hard-line network to allow 62 member utility companies to buy and sell small amount of surplus electricity.’⁷¹ His intention was to make it into an online exchange and expand its operation.⁷² In 2000, several companies joined with Sprecher to acquire Continental Power’s assets, and ‘[i]n May 2000 IntercontinentalExchange, LLC, was formed in Delaware.’⁷³ The company had ‘the goal of developing a platform to provide a more transparent and efficient market structure for OTC energy commodities trading.’⁷⁴

In 2001, ICE acquired IPE Holdings Plc, (the former International Petroleum Exchange), which allowed it to take on clearing services as well due to an existing arrangement with the London Clearing House.⁷⁵ It also meant that ICE was able to enter the futures markets for energy.⁷⁶

In 2005, ICE had its IPO on the NYSE.⁷⁷ At the time, ICE operated ‘futures markets, OTC markets and market data markets’.⁷⁸ The futures and OTC markets offered ‘derivative and physical products’ mainly in ‘contracts based on crude or refined oil, natural gas and power.’⁷⁹ The futures market was conducted through ICE Futures, a subsidiary part of the company located in London.⁸⁰ Until 2005, this had been an ‘open-outcry trading floor’, but ICE transformed it into a completely electronic exchange.⁸¹ ICE Data was formed in 2002, and was used to ‘compile[] and repackage[] trading data’ which could then be purchased by those interested in this information.⁸²

<http://money.cnn.com/2012/02/01/markets/nyse_uronext_deutsche_boerse/>; Aoife White and Nandini Sukumar, ‘Deutsche Boerse-NYSE Euronext Takeover Is Blocked by EU’, *Bloomberg* (online), 2 February 2012 <<http://www.bloomberg.com/news/articles/2012-02-01/european-commission-blocks-proposed-deutsche-boerse-nyse-uronext-merger>>.

⁷⁰ ‘IntercontinentalExchange, Inc’ in Jay P Pederson (ed), *International Directory of Company Histories, Volume 95* (St James Press, 2008), 205.

⁷¹ Ibid.

⁷² Ibid.

⁷³ Ibid.

⁷⁴ IntercontinentalExchange, Inc, *Form 10-K – Annual Report* (Company Report, 31 December 2005), 2 (‘*Annual Report*’).

⁷⁵ Ibid; ‘IntercontinentalExchange, Inc’, above n 70.

⁷⁶ IntercontinentalExchange, Inc, *Annual Report*, above n 74.

⁷⁷ Ibid 7.

⁷⁸ Ibid 3.

⁷⁹ Ibid 2-3.

⁸⁰ Ibid 3.

⁸¹ Ibid.

⁸² Ibid 4.

In 2007, ICE completed an acquisition of the New York Board of Trade which became ICE Futures U.S.⁸³ They also acquired the Winnipeg Commodity Exchange, which became ICE Futures Canada.⁸⁴ Both of these acquisitions provided greater diversity in the products which ICE traded.⁸⁵ Ice also turned ICE Futures into an electronic exchange.⁸⁶

In 2013, ICE acquired NYSE Euronext.⁸⁷

II RELAUNCHING EURONEXT N.V.

Following the merger of NYSE Euronext and ICE restructured Euronext so as ‘to separate the continental European operations of Legacy Euronext from ICE, and spin off the Group as an independent, publicly traded company by means of the IPO’.⁸⁸ This IPO took place in 2014,⁸⁹ and ICE later sold its remaining shares in Euronext.⁹⁰ Euronext N.V. has been listed on each of Euronext Paris, Euronext Amsterdam and Euronext Brussels.⁹¹ It now operates its business in: ‘listing, cash trading, derivatives trading, market data & indices, post-trade and Market Solutions & Other.’⁹²

G.4 Australian Securities Exchange

I EMERGENCE OF A NATIONAL EXCHANGE

During the 19th century, there were several state based exchanges in existence, most of which were located in capital cities.⁹³ Following the federation of the Commonwealth in 1901, the state exchanges held a conference in 1903, and ‘continued to meet on an informal basis through 1936.’⁹⁴ In 1937, they formed the Australian Associated Stock Exchanges which ‘gradually adopted company listing requirements, uniform brokerage rules, and commission fee guidelines.’⁹⁵ In 1960, the Sydney Greasy Wool Futures Exchange was established, eventually becoming the Sydney Futures Exchange in 1972, after having ‘diversified into a broader range of commodities such as beef, live cattle, and gold.’⁹⁶

The Australian Parliament incorporated the Australian Stock Exchange Limited in 1987, merging the six existing state exchanges together.⁹⁷ The ASX also launched its own electronic trading system SEATS (Stock Exchange Automated Trading System) in the same

⁸³ IntercontinentalExchange, Inc, *Annual Report*, above n 74, 7.

⁸⁴ Ibid.

⁸⁵ Ibid.

⁸⁶ Ibid.

⁸⁷ IntercontinentalExchange, Inc, *Annual Report*, above n 74, 7.

⁸⁸ Prospectus (Listing of Euronext on Euronext Lisbon 2014), 51.

⁸⁹ Ibid; Intercontinental Exchange, Inc, ‘Annual Report on Form 10-K’ (31 December 2014), 6.

⁹⁰ IntercontinentalExchange, Inc, *Annual Report*, above n 74, 6.

⁹¹ Prospectus (Listing of Euronext on Euronext Lisbon 2014), 51.

⁹² Euronext, ‘2014 Registration Document’ (Financial Report, 24 March 2015), 15.

⁹³ ‘ASX Limited’ in Thomas Derdak and Gretchen Antelman (eds), *International Directory of Company Histories, Volume 115* (St James Press, 2010), 34.

⁹⁴ Ibid 35.

⁹⁵ Ibid.

⁹⁶ Ibid.

⁹⁷ Ibid 36.

year.⁹⁸ This coincided with Black Monday in the U.S., which was a major crash in world markets, though neither ASX nor SFE closed.⁹⁹

The SFE launched SYCOM in 1989, which allowed it to offer ‘after-hours electronic trading.’¹⁰⁰ ASX closed its trading floors in 1990, with all trading to take place through SEATS.¹⁰¹ ‘In 1991 SFE established the subsidiary SFE Clearing House as a financial facility for settling, clearing, and maintaining a record of futures trades, and the following year, the New Zealand Futures and Options Exchange became a wholly owned subsidiary of SFE.’¹⁰² ‘In 1994 ASX introduced its broker-sponsored system of handling shares for a client, Clearing House Electronic Sub-register System (CHESS), which provided the exchange with its central register for share-ownership transfer.’¹⁰³

II DEMUTUALISATION AND LISTING

In 1998, ASX ‘was the first exchange in the world to demutualise and list on its own market.’¹⁰⁴ ‘In 1982, the then Trade Practices Commission ruled that stock exchanges must admit corporations as members. These corporations came to dominate trading, and in the 1997-98 financial year were responsible for 99 per cent of transactions on the equities market [...] A fundamental question facing ASX was whether there were inefficiencies inherent in this mutual structure inhibiting its ability to meet current and future challenges, such that there was a need to reform structural arrangements.’¹⁰⁵ Following a task force review and the recommendation of the Board, the resolutions required for demutualisation were passed in 1996.¹⁰⁶ The federal government then enacted the Corporations Law Amendment (ASX) Bill in 1997 to allow for both the demutualisation and listing to proceed, which took place in the next year.¹⁰⁷

While it had transformed into a publicly listed company, the ASX retained its supervisory role,¹⁰⁸ and in 2002, ‘the Australian Securities & Investments Commission (ASIC) called for ASX to adopt stricter standards in governing corporations, suggesting ASX’s need to produce profits hampered its regulation of its market. In 2004 ASX formed a Market Integrity Division to review and modify exchange practices used to supervise the market.’¹⁰⁹

III ACQUISITION OF SFE AND OTHER DEVELOPMENTS

⁹⁸ Ibid.

⁹⁹ ‘ASX Limited’, above n 93, 36.

¹⁰⁰ ASX, *History* <<http://www.asx.com.au/about/history.htm>>; see also ‘ASX Limited’, above n 93, 36.

¹⁰¹ Ibid.

¹⁰² ‘ASX Limited’, above n 93, 36.

¹⁰³ Ibid.

¹⁰⁴ ASX, *History*, above n 100; see also ‘ASX Limited’, above n 93, 36.

¹⁰⁵ ASX, ‘Annual Report’ (Company Report, 1998), 8 (‘Annual Report 1998’).

¹⁰⁶ Ibid; ‘ASX Limited’, above n 93, 36.

¹⁰⁷ ASX, ‘Annual Report 1998’, above n 105; ASX, ‘Annual Report’ (Company Report, 1999); ‘ASX Limited’, above n 93, 36.

¹⁰⁸ ASX, ‘Annual Report 1998’, above n 105, 9.

¹⁰⁹ ‘ASX Limited’, above n 93, 37.

Although a merger with SFE was proposed in 1999, this failed to take place, and it wasn't until 2006 that ASX acquired the SFE.¹¹⁰ 'Soon after the merger the company created ASX Markets Supervision to carry out its exchange-supervisory role and introduced real-time indices for gold and for metals and mining. ASX also supplanted the SEATS trading system with the new CLICK XT, an integrated platform for cash-equity and equity-derivative product trades.'¹¹¹

From 2007-2008, three companies applied for licenses to establish exchanges in Australia: Liquidnet Australia, AXE ECN, and Chi-X Australia.¹¹²

In 2010, ASX Market Supervision was renamed 'ASX Compliance Pty Limited to reflect the transfer of responsibility for market supervision to the Australian Securities and Investments Commission (ASIC).'¹¹³ ASX also employed 'ASX Group [as] the new master brand'¹¹⁴ for their different subsidiaries.¹¹⁵

G.5 NASDAQ

The Bunker Ramos Corporation designed NASDAQ (National Association of Securities Dealers Automated Quotations) to provide the NASD (National Association of Securities Dealers) with 'a national automated stock quotation system'¹¹⁶ for the OTC market.¹¹⁷ NASDAQ was implemented in 1971, and throughout the 1970s and 1980s transformed 'from a computer bulletin board service into an electronic stock market.'¹¹⁸

During the 1990s, NASDAQ experienced problems with 'abuses from market makers'¹¹⁹, and '[i]n July 1996 the U.S. Justice Department charged two dozen NASDAQ securities firms with "fixing transactions costs."¹²⁰ The SEC introduced regulatory changes in 1997 that were designed to increase transparency.¹²¹ 'Despite the bad publicity received by dealers, the NASDAQ's reputation did not suffer much damage. NASDAQ continued to soar in the second half of the 1990s, fueled [sic] by the growth of high-technology stocks and the allure of anything associated with the Internet.'¹²²

Prior to 2007, NASDAQ did not have its own national securities exchange status. It operated as a subsidiary of NASD, through delegation of its legal authority.¹²³ In 2000, NASDAQ took

¹¹⁰ ASX, 'Annual Report 1998', above n 105, 37; ASX, *History*, above n 100.

¹¹¹ ASX, 'Annual Report 1998', above n 105, 37-38.

¹¹² Ibid 38.

¹¹³ ASX, 'Annual Report', (Company Report, 2011), 36; ASX, *History*, above n 100.

¹¹⁴ ASX, 'Annual Report', (Company Report, 2010), 31.

¹¹⁵ Ibid; ASX, *History*, above n 100.

¹¹⁶ 'The NASDAQ Stock Market, Inc' in Tina Grant (ed), *International Directory of Company Histories, Volume 92* (St James Press, 2008) 257.

¹¹⁷ Ibid 256-57.

¹¹⁸ Ibid 257-58.

¹¹⁹ Ibid 258.

¹²⁰ Ibid.

¹²¹ Ibid.

¹²² Ibid.

¹²³ Nasdaq Stock Market, Inc, 'Form 10-K – Annual Report' (Company Report, 31 December 2001), 5.

steps to transform from being ‘a wholly-owned subsidiary¹²⁴ of NASD to an independent exchange operator. NASDAQ applied to ‘the SEC for registration as a national securities exchange’,¹²⁵ which would be required for Nasdaq to operate as an exchange independently of the NASD. While this process took place, NASDAQ underwent ‘a two-phase private placement of securities commencing in June 2000.’¹²⁶ Common stock began to be traded in 2002 through NASDAQ’s OTC Bulletin Board.¹²⁷

‘FINRA [(previously the NASD)] fully divested its ownership of Nasdaq in 2006, and The NASDAQ Stock Market became fully operational as an independent registered national securities exchange in 2007.’¹²⁸

Another significant event was the merger with OMX AB in 2008 to become The NASDAQ OMX Group, Inc.¹²⁹

G.6 TMX Group Inc.

In 1852, an “Association of Brokers” met in Toronto, which would become the Toronto Stock Exchange in 1861.¹³⁰ This was ‘a not-for-profit organization that was owned by its members’¹³¹ and was incorporated in 1878.¹³² In the same year ‘it moved into its first permanent headquarters in Toronto.’¹³³ During the 20th century, the exchange generally experienced growth, ‘despite a recession that followed World War I and a global recession that extended throughout the 1930s.’¹³⁴

TSE ‘introduced the Computer Assisted Trading System (CATS), the world’s first electronic trading platform’¹³⁵ in 1977.¹³⁶ In 1996, it ‘closed[d] its trading floor by implementing complete automated trading.’¹³⁷ In 1997, TSE adopted a new system operated by the Paris Bourse, as CATS was no longer capable of meeting the demands of the market.¹³⁸

A scandal caused by Bre-X Mineral Ltd. in 1997 also affected the exchange.¹³⁹ ‘The company’s claim to have discovered the world’s largest gold deposit was shown to be fraudulent during the spring of 1997. While investors lost millions of dollars, the exchange

¹²⁴ Ibid 3.

¹²⁵ Ibid 4.

¹²⁶ Ibid; ‘The NASDAQ Stock Market, Inc’, above n 116, 259.

¹²⁷ Nasdaq Stock Market, Inc, ‘Form 10-K – Annual Report’ (Company Report, 31 December 2002), 4.

¹²⁸ NASDAQ OMX Group, Inc, ‘Form 10-K– Annual Report’ (Company Report, 31 December 2014), 2.

¹²⁹ Ibid.

¹³⁰ ‘TMX Group Inc’ in *International Directory of Company Histories, Volume 136* (St James Press, 2012), 453.

¹³¹ Ibid.

¹³² Ibid.

¹³³ Ibid.

¹³⁴ Ibid 453-54.

¹³⁵ Ibid 454.

¹³⁶ Ibid.

¹³⁷ Ibid.

¹³⁸ Ibid.

¹³⁹ Ibid.

was tarnished by its association with the scandal. A year later TSE raised the listing requirements for mining and exploration companies.¹⁴⁰

The demutualisation and listing of the TSE took place following a realignment of Canadian exchanges:¹⁴¹ ‘Toronto Stock Exchange for senior equities, and CDNX for junior equities, with the Bourse de Montreal concentrating exclusively on derivatives.’¹⁴² Then in 2000, the TSE became a ‘private, for-profit company’¹⁴³ that went on to acquire the CDNX in 2001, which ‘was renamed the TSX Venture Exchange.’¹⁴⁴ In 2002, TSE ‘adopted the TSX acronym’¹⁴⁵ and the TSX Group listed itself on the TSX.¹⁴⁶

‘Since 1999 TSX and the Montreal Exchange had abided by a 10-year noncompete agreement, but as that arrangement neared its end, both parties had to consider their next step. Rather than face additional competition, they decided to join forces, and in late 2007 they announced a merger agreement that would result in an integrated exchange operation called TMX Group Inc.’¹⁴⁷

In 2011, an attempted merger with the LSE did not go ahead.¹⁴⁸

G.7 SGX

I ORIGINS

Trading in stocks resulted from the work of commodity brokers in British Malaya.¹⁴⁹ Most of it was conducted in Singapore and the Singapore Stockbrokers Association was registered in 1930.¹⁵⁰ ‘This became the Malayan Stockbrokers Association in 1938 to reflect the Malayan character of the organisation. As a society, the Association regulated its own affairs with minimal governmental interference.’¹⁵¹

In 1960, the Malayan Stock Exchange was created with a trading room in each of Singapore and Kuala Lumpur.¹⁵² ‘In 1963, it became the Stock Exchange of Malaysia. When Singapore became independent in 1965, the Stock Exchange was re-named once more, becoming the Stock Exchange of Malaysia and Singapore.’¹⁵³ The Stock Exchange of Singapore Ltd was incorporated in 1973, separating itself from Malaysia.¹⁵⁴

¹⁴⁰ Ibid.

¹⁴¹ Ibid; TSX, ‘Annual Report’ (Company Report, 2002), 15 (‘Annual Report 2002’).

¹⁴² TSX, ‘Annual Report 2002’, above n 141.

¹⁴³ Ibid 15.

¹⁴⁴ ‘TMX Group Inc’, above n 130, 454; TSX, ‘Annual Report 2002’, above n 141, 15.

¹⁴⁵ ‘TMX Group Inc’, above n 130, 455.

¹⁴⁶ Ibid; TSX, ‘Annual Report 2002’, above n 141, 14-15, 17, 27.

¹⁴⁷ ‘TMX Group Inc’, above n 130, 455.

¹⁴⁸ Ibid.

¹⁴⁹ Walter Woon (ed), *Butterworths Handbook of Singapore Securities Law* (Butterworths Asia, 1998), 1.

¹⁵⁰ Ibid.

¹⁵¹ Ibid.

¹⁵² Ibid.

¹⁵³ Ibid.

¹⁵⁴ Ibid.

The exchange was largely self-regulated until Pan-Electric Industries collapsed in 1985, prompting the closure of both the Singapore and Kuala Lumpur Stock Exchanges for three days.¹⁵⁵ The Securities Industry Act 1986 placed supervision of the securities industry under the Monetary Authority of Singapore.¹⁵⁶ In 1990, companies based in either Malaysia or Singapore delisted from each other's exchange.¹⁵⁷

II DEMUTUALISATION AND MERGER TO FORM SGX

'In October 1998, the Committee on the Governance of Exchanges (CGE) consisting of representatives from the private and public sectors, submitted its report. It recommended the demutualisation of the two legacy exchanges – the Stock Exchange of Singapore (SES) and the Singapore International Monetary Exchange (SIMEX) – simultaneously with their merger.'¹⁵⁸

This took place in 1999 with the creation of SGX.¹⁵⁹ In 2000, SGX then listed itself on its own exchange.¹⁶⁰

G.8 Hong Kong Stock Exchange

I ORIGINS

Securities trading in Hong Kong could be traced back to 1860s.¹⁶¹ This was the period when Hong Kong started to prosper, with the enactment of the Hong Kong's first Companies Ordinance allowing the formation of companies with limited liability.¹⁶² In the same decade, one of the most important corporations in Hong Kong's history was formed – the Hongkong and Shanghai Banking Corporation (HSBC).¹⁶³

However, it was not until 1891 the first formal stock exchange was established, the Association of Stockbrokers in Hong Kong.¹⁶⁴ The Association was renamed the Hong Kong Stock Exchange in 1914.¹⁶⁵ The exchange in its early days was comprised of expats and had no Chinese members. On October 1, 1921, an all-Chinese stock exchange, the Hong Kong Sharebrokers' Association, was established for the Chinese community.¹⁶⁶

¹⁵⁵ Ibid 2.

¹⁵⁶ Ibid 2.

¹⁵⁷ Ibid 2-3.

¹⁵⁸ SGX, 'Annual Report' (Company Report, 2000), 10.

¹⁵⁹ Ibid.

¹⁶⁰ Ibid 6-7.

¹⁶¹ Hong Kong Securities and Clearing Limited, 'A Glimpse of the Past' (Report, May 2011), 1.

¹⁶² Ibid.

¹⁶³ Ibid.

¹⁶⁴ Ibid.

¹⁶⁵ Ibid.

¹⁶⁶ Ibid.

The two exchanges merged into one after the Second World War, due to low volume of trading at the time and expensive transaction fee.¹⁶⁷

The rapidly blooming of economy in Hong Kong in the early 1960s, in particular with the vast development of infrastructure and the financial sector, paved the way to prosperity in Hong Kong. The Hang Seng Index (HSI) became public on November 24, 1969.¹⁶⁸ Three more exchanges established in the same period – the Far East Exchange (1969), the Kam Ngan Stock Exchange (1971) and the Kowloon Stock Exchange (1972).¹⁶⁹

In the early days of securities trading in Hong Kong, there were no disclosure rules and insider dealing was common.¹⁷⁰ The Hong Kong stock market and economy peaked in 1973 before plummeting in 1974.¹⁷¹ In response to the crashing of the market, the Securities Ordinance and the Protection of Investors Ordinance were enacted to protect investors.¹⁷²

In 1976, the Hong Kong Commodity Exchange was established as a trading venue for products such as cotton futures, sugar futures, soybean futures and gold futures.¹⁷³ It was renamed the Hong Kong Futures Exchange (HKFE) on May 7, 1986.¹⁷⁴

Since 1977, there were talks about consolidating the four exchanges.¹⁷⁵ However, it was not till March 27, 1986 before all four exchanges ceased operation and become the Stock Exchange of Hong Kong (SEHK).¹⁷⁶ The unified exchange commenced trading on April 2 in the same year.

II OTHER SIGNIFICANT EVENTS AND DEVELOPMENTS

On Monday October 19, 1987, the Hong Kong market plunged following the global markets crashed on Black Friday (October 16).¹⁷⁷ The stock exchange was immediately suspended for four days from October 20 to October 23. The market continued to dive 43 per cent the day on which the exchange was reopened.¹⁷⁸

Ten years later, in 1997, after the HSI reached a long term high of 16820.31 points on August 7, the stock market crashed again in October after the Asian Financial Crisis struck.¹⁷⁹ The HSI fell to all time low at 6544.79 on August 13, 1998.¹⁸⁰ The Hong Kong Government intervened by injecting \$120 billion HKD to stabilise the market.¹⁸¹

III DEMUTUALISATION AND MERGER OF EXCHANGES

¹⁶⁷ Ibid.

¹⁶⁸ Ibid 2.

¹⁶⁹ Ibid.

¹⁷⁰ Ibid 1.

¹⁷¹ Ibid 2-3.

¹⁷² Ibid 3.

¹⁷³ Ibid.

¹⁷⁴ Ibid.

¹⁷⁵ Ibid 4.

¹⁷⁶ Ibid.

¹⁷⁷ Ibid.

¹⁷⁸ Ibid.

¹⁷⁹ Ibid 6.

¹⁸⁰ Ibid 7.

¹⁸¹ Ibid.

In March 2000, SEHK, HKFE and the Hong Kong Securities Clearing Company were demutualised and subsequently merged to form the Hong Kong Exchanges and Clearing Limited (HKEx).¹⁸²

IV COLLABORATION WITH OTHER EXCHANGES

In recent years, HKEx is working closely with stock exchanges in China. A Closer Cooperation Agreement (CCA) was entered into with Shenzhen Stock Exchange and the Shanghai Stock Exchange respectively on January 21, and April 8, 2009.¹⁸³ On November 17, 2014, the Shanghai-Hong Kong Stock Connect was launched and further opened up the Chinese market for foreigners to purchase A shares listed in Shanghai and for mainland Chinese investors to buy authorised shares of Hong Kong and Chinese companies listed in Hong Kong.¹⁸⁴

In December 2012, HKEx acquired the London Metal Exchange and entered the base metals market.¹⁸⁵

G.9 Shanghai Stock Exchange & Shenzhen Stock Exchange

I HISTORY OF CHINESE STOCK MARKET

The earliest form of shares trading in China dated back to the 1860s. Evidence of trading could be found in *The North-China Herald* in 1866 with a list of ‘Shares and Stocks’ under the title of ‘Monetary & Commercial’. It was not till 1871 before a system of trading, despite small scale, was developed.¹⁸⁶ Formal exchanges were only developed after the 1911 Revolution after gaining government support.¹⁸⁷

The market began its downfall in 1937, when the second Sino-Japanese War erupted after the 7 July incident on the Marco Polo Bridge. On August 13, 1937, the government closed the Exchange. The war continued for eight years and ended in 1945. During the early years of war, however, ‘black bourse’ was developed and trading continued.

Alongside with the ‘black bourse’, the Shanghai Chinese Stock Exchange was open in December 1940 and the Chinese Merchants Securities Exchange in November 1943. A continuous rise in the markets was reported until early 1945¹⁸⁸. The market responded positively to the news of the surrender of the Japanese forces, and share prices went to all

¹⁸² Ibid 9.

¹⁸³ Ibid 14.

¹⁸⁴ Goldman Sachs, ‘China is Transforming the Global Economy – The Shanghai-Hong Kong Stock Connect’ (News, November 2014) <<https://www.goldmansachs.com/our-thinking/pages/stock-connect/>>.

¹⁸⁵ Hong Kong Securities and Clearing Limited, *History* <<https://www.hkex.com.hk/eng/exchange/corpinfo/history/history.htm>>.

¹⁸⁶ William Thomas, *Western Capitalism in China* (Ashgate, 2001) 118.

¹⁸⁷ Ibid 245.

¹⁸⁸ Ibid 266.

time high. However, soon after, investors started selling off shares to settle debt and that led to the collapse of the market.¹⁸⁹

In September 1946, the official, formal and regulated Exchange was reopened – the Shanghai Securities Exchange. However, a combination of commercial uncertainty and high interest rate, the stock exchange never flourished again before the Exchange came to an ‘abrupt halt’ in 1949 due to the interference of the Communist Party took over the country. By that time, most of the foreign investors have left Shanghai and all registered companies ceased operation or became ‘nationalised’.¹⁹⁰

II THE ESTABLISHMENT OF THE SHANGHAI STOCK EXCHANGE

The Shanghai Stock Exchange was officially established on 26 November 1990 after fifty years since there was once an official stock exchange in China. It came into operation on 19 December 1990.¹⁹¹ It is a self-regulated and mutualised institution.¹⁹² Initially, it had 25 brokerage firms as members and had no foreign participation.¹⁹³ The Shanghai market was one of the two markets permitted by the Government to trade shares (the other being Shenzhen).

In July 15, 1991, the first stock index was launched by the SSE, which was being replaced by the SSE 30 index on July 1, 1996.¹⁹⁴ In December 1993, SSE was transformed into a nation-wide market.

The exchange is under the supervision of China Securities Regulatory Commission (CSRC), whose role is to provide regulatory oversight on securities and futures markets in China.

The SSE is the most preeminent stock market in Mainland China. It has the most number of listed companies.¹⁹⁵ In 2013, it has a market capitalisation of RMB 15,116.53 billion.¹⁹⁶

The SSE expanded tremendously in mid 90s. The first surge in listing occurred in 1993-1994, until credit restrictions were imposed by the Government to slow economic growth. The market capitalisation ranking of the two exchanges, calculated by the World Bank’s International Finance Corporation, was in the 17th place in 1997.¹⁹⁷

The market in Shanghai is segmented. There are a number of different types of stock exchange membership and company capital is categorised as A shares for domestic holders, B shares for overseas holders, H shares for shares listed in Hong Kong and N shares for shares listed in New York.

III THE ESTABLISHMENT OF SHENZHEN STOCK EXCHANGE

¹⁸⁹ Ibid 266 n 94.

¹⁹⁰ Ibid.

¹⁹¹ Shanghai Stock Exchange, *Brief Introduction* <<http://english.sse.com.cn/aboutsse/sseoverview/brief/>>.

¹⁹² Ibid.

¹⁹³ Thomas, above n 186, 280.

¹⁹⁴ Shanghai Stock Exchange, *Timeline* <<http://english.sse.com.cn/aboutsse/sseoverview/timeline/>>.

¹⁹⁵ Shanghai Stock Exchange, *Brief Introduction* <<http://english.sse.com.cn/aboutsse/sseoverview/brief/>>.

¹⁹⁶ Ibid.

¹⁹⁷ Thomas, above n 186, 281.

Shenzhen Stock Exchange (SZSE) established on December 1, 1990.¹⁹⁸ The exchange is self-regulated, but the China Securities Regulatory Commission (CSRC) provides the oversight to the exchange.¹⁹⁹

The SZSE has become interested in collaborating with exchanges worldwide and has since signed memoranda of understanding (MOUs) with more than over 30 major stock exchanges.²⁰⁰ One of the earliest MOUs was signed in Beijing on June 20, 1993 to enhance cooperation in regulatory oversight with the CSRC, the Hong Kong Securities and Futures Commission (SFC), the Stock Exchange of Hong Kong (SEHK) and the Shanghai Stock Exchange (SSE).²⁰¹

The market in China continued to open up to foreigners. On August 20, 1993, the SZSE granted special seats to eight overseas licensed brokers to trade B-shares at the exchange.²⁰²

On September 19, 1996, SZSE joined the IOSCO as an affiliate member and was on the organisation's Consultative Committee.²⁰³

In 1997, the exchange became fully electronic and abolished its trading floor.²⁰⁴

On April 8, 2005, the Shanghai and Shenzhen 300 Index (CSI Index) was officially launched.²⁰⁵

In 2009, ChiNext was established and October 30, 2009 the first 28 ChiNext issuers were listed on the SZSE.²⁰⁶ On June 1, 2010, the ChiNext index was launched. In the same year, SZSE had the highest number of initial public offerings (IPOs) among all stock exchanges worldwide with 321 IPOs.²⁰⁷

¹⁹⁸ Shenzhen Stock Exchange, *SZSE Overview* < <http://www.szse.cn/main/en/AboutSZSE/SZSEOverview/>>.

¹⁹⁹ Ibid.

²⁰⁰ Ibid.

²⁰¹ Shenzhen Stock Exchange, *Milestones* < <http://www.szse.cn/main/en/AboutSZSE/Milestone/>>.

²⁰² Ibid.

²⁰³ Ibid.

²⁰⁴ Ibid.

²⁰⁵ Ibid.

²⁰⁶ Ibid.

²⁰⁷ Ibid.

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