

MEMO# 35954

December 13, 2024

IOSCO Publishes Final Report on Exchange Operation, Governance, and Business Models

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TO: ICI Members
ICI Global Members
Derivatives Markets Advisory Committee
Equity Markets Advisory Committee
SUBJECTS: International/Global
Trading and Markets
RE: IOSCO Publishes Final Report on Exchange Operation, Governance, and Business Models

On 29 November, the International Organization of Securities Commissions (IOSCO) published a final report on the evolution of exchange operation, governance, and business models.[\[1\]](#)

IOSCO describes exchanges as "lynchpins of the financial system"[\[2\]](#) with the focus of the report being on equity exchanges. IOSCO notes, however, that the report may be relevant to other types of trading venues and trading in other classes of financial instruments such as exchange-traded funds, bond, and derivatives.

The Report follows a consultation published earlier this year.[\[3\]](#) IOSCO received 20 responses, including a high-level response from ICI that offered support for the work and the need for IOSCO's involvement in this area.[\[4\]](#) I

The Report reviews and analyses changes in exchange structure and organisation, focusing on business models and ownership structures. It then considers the impact of such changes, particularly shifts to cross-border operations within large corporate groups. The Report provides considerations for regulators, including risks and challenges of supervising exchanges within different types of organisational structures. IOSCO describes good supervisory practices for assessing the organisational structure of exchanges and exchange groups, the supervision of exchanges and other trading venues within exchange groups, and the supervision of multinational exchange groups.

These practices are intended to be high-level and outcome-focused, rather than granular and prescriptive. The Report was amended to clarify that approaches should be tailored,

with each authority identifying the most appropriate tools for the legal framework in that jurisdiction.

Developments in Exchange Structure and Organization

The Report describes recent developments in the business models and structures of exchanges and secondary markets. These changes include demutualisation, consolidation through acquisitions, and incorporation into larger corporate groups. The result of such changes has been increases in interconnections and cross-border activities. In addition, exchanges have new business lines, some individually and some through affiliates in corporate groups.

Respondents generally agreed with IOSCO's observations of these developments, but some minor adjustments were made to the Report were made to reflect feedback. The Report reflects additional factors leading to the trend of demutualisation, including rising capital costs in technology, which increases the importance of scale. The role of increased competition was also included and addresses perceptions of an unlevel playing field between exchanges and other trading venues (i.e., between "lit and dark trading platforms").

Proposed Good Practices and Tools

The Report identifies risks and challenges associated with exchange structure and organisation, which follow from the demutualisation trend. Although many respondents to the Consultation expressed the view that these risks as mitigated, the Report focuses on a set of common good practices for regulators that can broadly improve risk mitigation and supervision.

The good practices seek to:

- Ensure the autonomy and independence of decision-making at the individual exchange, even where part of a larger corporate group.
- Assess whether exchanges have put in place compliance arrangements and policies for relevant regulatory obligations and individual exchanges have sufficient expertise.
- Assess potential conflicts of interest that may arise (i) between an individual exchange and an exchange group and (ii) between managing commercial interests and regulatory obligations.

In the management of exchanges, the Report recognises concerns regarding potential monopolistic risks and identifies several potential conflicts of interest that warrant supervisory focus and examples of tools that may be used to mitigate such conflicts. These concerns include:

- "Dual hatting," a practice in which individuals within an exchange group may hold positions at multiple entities. Mitigating tools include ownership and voting limits, restrictions on the composition or structure of the board, independent directors, provisions that require fair representation of stakeholders on the board, and fitness requirements for board members.
- Multiple reporting lines, with managers of the exchange also functioning as managers at another level of the corporate group. Mitigating tools include establishing the exchange as an independent entity or wholly owned subsidiary with a separate management and board, requiring exchange functions be performed by a registered exchange, and requiring exchanges to establish and enforce organisational and

trading rules.

- Intragroup servicing, where activities or responsibilities for the group are performed by a single entity, such as the parent company or shared service centre, rather than at the exchange. Mitigating tools include strict framing and consistent supervision of outsourcing or delegation arrangements, requiring arrangements to be monitored and reported to senior levels within the exchange, and other regulatory limits.
- Financial resources management, where cash pooling might be used to balance funds within a corporate group. Mitigating tools include regular regulatory submissions of audited financial statements or budgets, maintenance of reserve funds, and restrictions on use of regulatory funds.
- Carrying out other activities, where exchanges or the subsidiaries or affiliates carry out activities that might not be regulated such as data processing and data analytics, developing indices and other benchmarks, and technology services. Mitigating tools include additional financial resource requirements; disclosures to ensure client understanding of regulated and non-regulated activities; and requiring regulatory notice for additional services.

IOSCO acknowledges that jurisdictions have regulatory requirements specifically designed to address these risks while ensuring that markets remain competitive.

Regulators should assess the effectiveness of arrangements for market operations, including conflicts of interest management, corporate and operational governance, and trading transparency. Supervisors should also ensure that there are processes and arrangements in place to address changes to corporate structure and any resulting potential conflicts of interest. Regulators may use a variety of tools to address these issues such as requiring exchange operations to be consistent with public interest, reporting requirements, funding requirements/restrictions, ownership limitations, and physical presence requirements. IOSCO received some practical feedback on these practices, incorporating additional supervisory practices including a Code of Conduct, periodic reporting, or independent directors, and presence of Public Interest Directors as means within the toolkit of avoiding conflicts of interest.

Multinational exchange group supervision raises additional regulatory concerns because of differences in legal frameworks and the need for cross-border supervision for outsourcing. IOSCO proposes that regulators consider using memoranda of understanding, supervisory colleges, and regulatory networks to facilitate cross-border regulatory and supervisory cooperation. These tools may also enable regulators to monitor developments in the structure of and ownership of multinational groups to ensure adequate supervision in relevant jurisdictions. Licensing requirements may also be a useful tool to ensure adequate supervision.

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Notes

[1] IOSCO, [Evolution in the Operation, Governance, and Business Models of Exchanges: Regulatory Implications and Good Practices: Final Report](#) (29 November 2024) (the Report).

[2] Report at 7.

[3] IOSCO, [Evolution in the Operation, Governance and Business Models of Exchanges: Regulatory Implications and Good Practices: Consultation Report](#) (4 April 2024) (the Consultation).

[4] [Letter from Annette Capretta to IOSCO, Re: Evolution in the Operation, Governance and Business Models of Exchanges: Regulatory Implications and Good Practices](#) (3 July 2024).

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