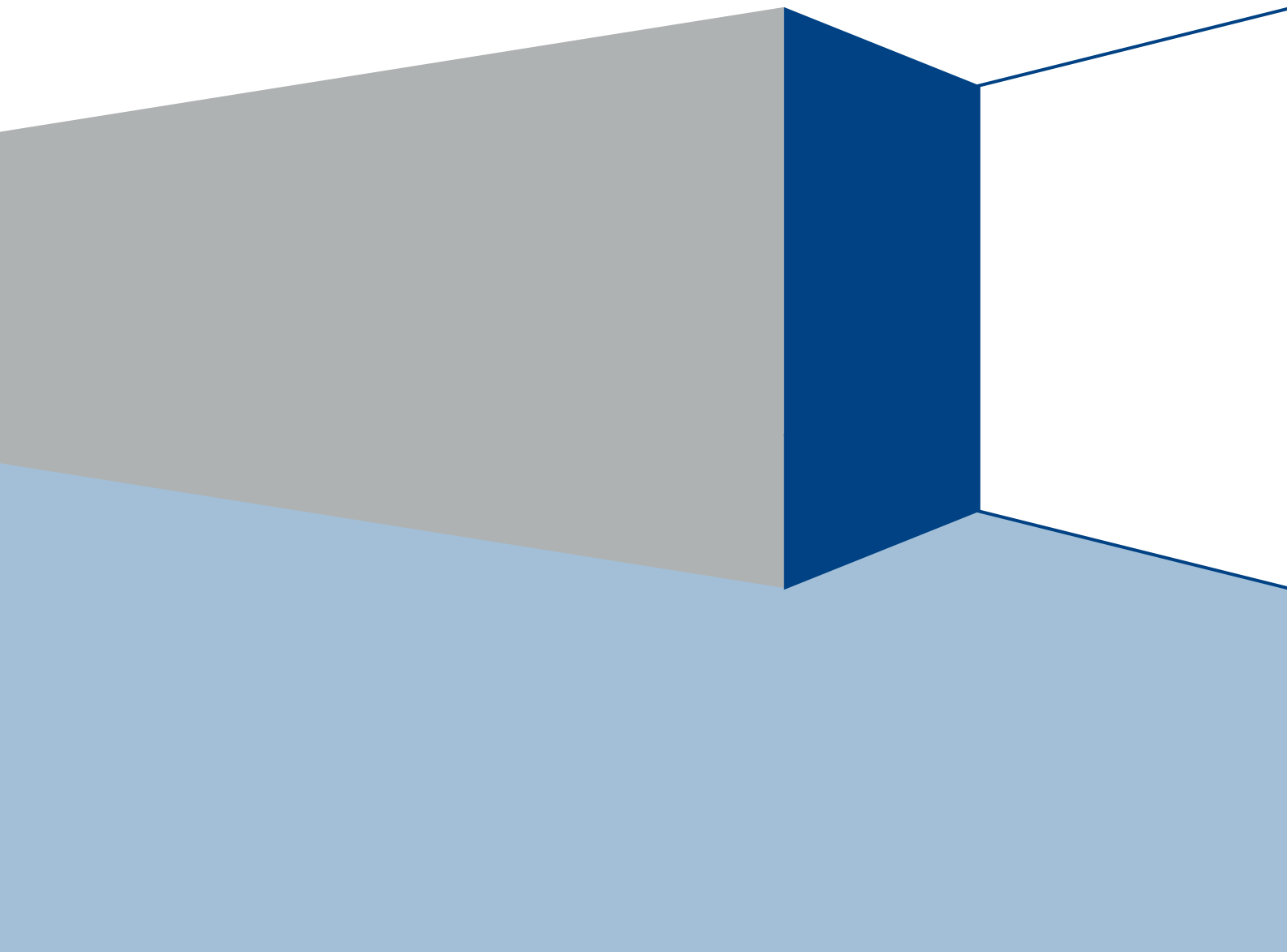




London
Stock Exchange

CONSULTATION JUNE / JULY 2009

International Order Book



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1 Introduction

The International Order Book (IOB) enables investors to unlock the potential of some of the world's fastest growing markets. It offers easy and cost efficient access to markets around the world via depositary receipts (DRs).

The market has grown rapidly since its inception with some of the most heavily traded securities on the London Stock Exchange ("the Exchange") being traded on the IOB. To facilitate its continued growth, we have recently implemented a number of important changes, including introducing LCH.Clearnet Ltd ("LCH") as the central counterparty (CCP) for trades in the 50 most liquid securities and extending the market opening hours.

When these changes were made, the Exchange committed to holding a consultation to focus on certain aspects of the new services and to gain feedback from market participants.

1.1 Purpose of this document

The aim of this document is to consult on:

- The handling of corporate action events with options – see section 2
- The policy towards DR banks in respect of retrospective record dates – see section 3
- The opening hours of the market – see section 4
- The extension of IOB Clearing – see section 5
- The overall IOB service – see section 5

In this way the Exchange will ensure that it continues to offer its customers a world class market for DRs.

This document presents specific questions on which we would welcome feedback. Firms are requested to respond to these questions but are encouraged to comment more widely – the Exchange welcomes feedback on all our proposals to ensure we deliver optimum solutions for the whole market. Firms are also requested to collate comments from all relevant departments (front and back office) and submit a single consolidated response to this paper. A summary of the specific consultation questions is provided in section 6.

This consultation runs from Wednesday 17 June to Wednesday 15 July. Responses should be submitted by email to job@londonstockexchange.com.

1.2 Readership

This consultation document should be read by member firms and in particular those member firms operating as Clearing Members. It is also useful for prospective participants who may wish to commence trading on the IOB.

It should specifically be read by those departments that are involved with trading, clearing, settlement and risk.

1.3 Contact details

To contact the Exchange:

- Please contact your **Primary Account Manager** or Kara Hyne on +44 (0)20 7797 1608, khyne@londonstockexchange.com

To contact LCH:

- Please contact Andrew Rees on +44 (0)207 426 7469, andrew.rees@lchclearnet.com

Further information about the International Order Book can be found at <http://www.londonstockexchange.com/iob>

2 Corporate actions

2.1 Overview

The vast majority of corporate actions in IOB securities are processed without any issues arising. However, with the introduction of the CCP service, it is not possible to provide buyer protection facilities in relation to corporate actions with options, i.e. to allow the buyer of a security that is the subject of a corporate action with options to elect to accept any option apart from the default. This is in contrast to the service available for securities traded on SETS, for example, where buyer protection, via ACON functionality, is provided through Euroclear UK and Ireland.

Some member firms have requested that a solution be explored to allow buyers to request any option against an eligible outstanding transaction in the event of a relevant corporate action. This section of the consultation explores the option that has been put forward by LCH and the Exchange.

2.2 Current service

Currently, if a corporate action with options occurs on an IOB CCP security, trades are processed in the usual way by LCH and the default option is delivered to buyers if their trades were unsettled at the last time for acceptances to be made. Note that holders of DRs are able to elect on the full range of options in all cases.

The benefits of this service are that:

- The outcome of the trade is certain
- The process is simple and fully automated, unlike in the current OTC market
- Trades remain cleared by the CCP and subject to LCH rules, so market participants retain all of the benefits of a CCP. In particular, participants have complete certainty that there is no counterparty risk at any time when trading one of the CCP eligible securities on-book on the IOB
- As regards counterparties, participants only need a relationship with either LCH or a GCM

2.3 Alternative proposal

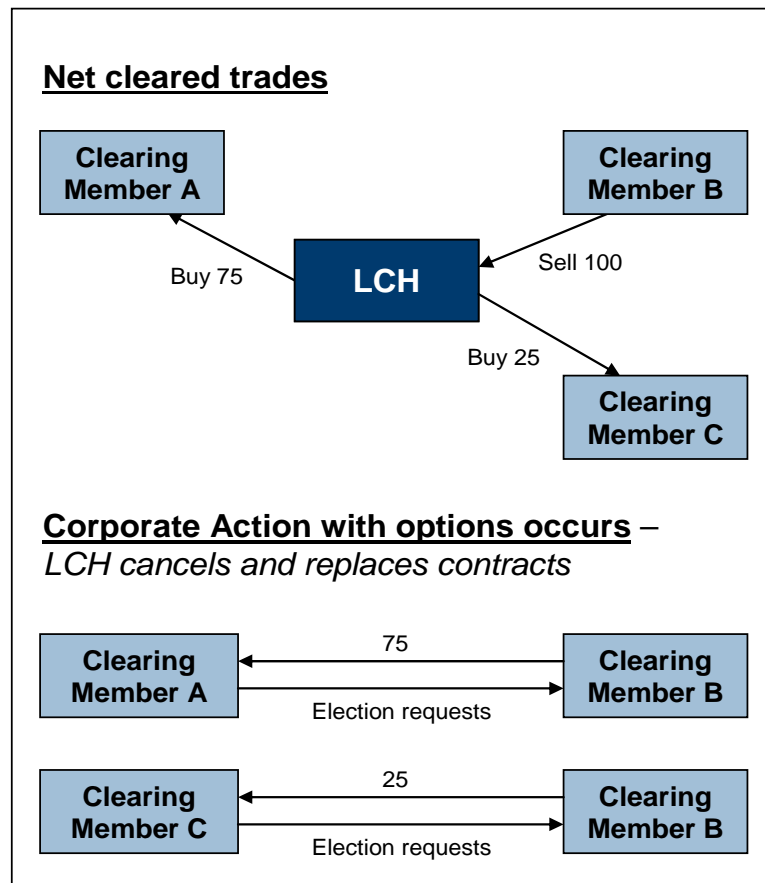
The objective of this proposal is to enable firms to obtain the benefit of the full range of options available in an applicable corporate action, using buyer protection instructions. This can only be achieved by the CCP stepping out of the relevant transactions where a corporate action with options occurs.

For certain corporate actions with options, the proposal is as follows:

For open positions:

Net or gross settlement positions would be cancelled between Clearing Members and LCH. They would be replaced by multilateral net settlement contracts created bilaterally between Clearing Members. Cancellation and replacement would be mandatory for all market participants who had open trades in the relevant security. The buying Clearing Member would then notify the selling Clearing Member of the option it, or its client, wished to select.

For example:



Such cancelling and replacement may give rise to differences in the consideration attaching to each contract. The Clearing House would settle this directly with Clearing Members via the Protected Payments System (PPS).

For settled entitled positions:

LCH would identify all the relevant entitled positions that settled prior to the date of cancellation and replacement. LCH would allocate buyers to sellers and send the information via notification to all relevant parties.

Allocation of entitlement to Clearing Members would be mandatory for all settled but entitled transactions.

LCH would impose a fee for this service which would be commensurate with its charge for a buy-in notice, plus an additional charge expected to be in the region of £125 per contract side in the first two years to cover LCH's initial development costs.

To put this issue in context, over the last two years, six corporate action events have occurred on the IOB which would have triggered this process had this proposal been in place.

Paragraphs 2.3.1 to 2.3.8 below set out the key features of the proposal and the issues to be considered. The Exchange is seeking participants' views on the proposal. To aid respondents, a number of specific questions are set out in this section. Participants are asked to confirm whether their overall preference is to retain the current service or to adopt the alternative proposal.

It should be noted that all aspects of this proposal are subject to regulatory approval and, depending on the outcome of this consultation, the Exchange and LCH will be required to develop detailed rules and additional arrangements that may be the subject of further consultation.

Question 1: Market participants are invited to comment on the proposal set out in sections 2.3.1 to 2.3.8. To be able to elect for options on applicable corporate actions, respondents should understand that under this proposal:

- ***all of their trades in affected securities will be subject to the cancellation and replacement process, even where the buyer wishes to elect for the default option normally provided by LCH;***
- ***they will be exposed to an element of counterparty risk;***
- ***they lose a degree of anonymity;***

- ***Clearing Members will be responsible for managing the settlement of the trades; and***
- ***they will be charged a cancellation and replacement fee, even if they want to accept the default option in an applicable corporate action.***

Taking into account all of the details of the alternative proposal, would respondents prefer to retain the current service or adopt this proposal?

2.3.1 Events subject to cancellation and replacement of contracts or entitlement notification to Clearing Members

The following events in particular would be subject to the cancellation and replacement process:

- Interim security subscriptions
- Tender offers / Takeovers / Purchase offers
- Rights issues without interim security

All other corporate action events would be processed as currently.

Where new event types arise or any doubt exists, LCH would at its absolute discretion determine any treatment. LCH would send cancelling and replacement or entitlement notification notices to its Clearing Members via the same channels used for LCH's Buying In notices (see section 2.3.3).

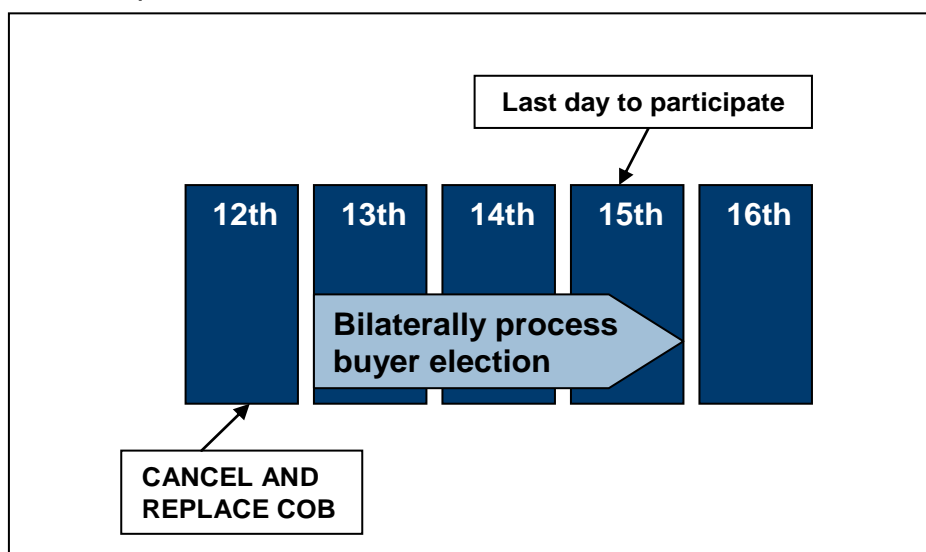
Question 2: Do respondents believe that there are other corporate action events that should be included in the proposal and why?

2.3.2 Date conventions for cancellation and replacement of contracts or entitlement notification to Clearing Members

Interim security subscriptions, tender offers, takeovers, purchase offers

Where the last day to participate is Y, cancelling and replacing to Clearing Members would take place based on all open or pending positions at close of business on Y-3.

For example:



Therefore in the example shown, all open or pending positions at close of business on the 12th would be cancelled and replaced by notification to Clearing Members (this would include all trades that were executed on 10th, 11th and 12th plus any trades that were executed before then but which have not yet settled). This may mean that trades due to settle normally on or before the last date for participation would be cancelled and replaced by notification to Clearing Members. However, it would allow participants three business days to contact their allocated counterparty and arrange the appropriate option. Trades conducted on or after the 13th would be subject to the normal CCP service.

If adequate notification of an event was given, the Exchange would aim to move the security that was the subject of the corporate action to the uncleared IOBU segment from close of business on the day of notification of the event until two days prior to the last day for participation. All trades that were executed in this security over this time period would be exposed to counterparty risk and would be settled bilaterally on a gross basis. However, participants should note that the Exchange rarely receives advance notice of these types of events and would therefore be unlikely to be able to move the security.

Question 3: Do respondents believe that all trades should be cancelled and replaced by notification to Clearing Members three days ahead of the last day to participate? If not what period would they suggest and why?

Rights issues without interim security

As holders are not required to elect an option prior to the ex date in these events, open cum positions would be cancelled and replaced by

notification to Clearing Members at close of business on ex date minus one or on the date the Stock Situation Notice was published by the Exchange, whichever was the later.

All trades executed on ex date minus one would be subject to being cancelled and replaced.

In the event of late notification of the record date, settled cum positions would be identified and have the entitlement allocated back to Clearing Members at the close of business on ex date minus one or on the date the Stock Situation Notice was published by the Exchange, whichever was the later. LCH would track or retrieve all trades between record and ex date, determine if they were entitled to take part in the event, and notify the entitlement to Clearing Members accordingly. All positions thus identified would be notified to Clearing Members.

2.3.3 Notification of cancellation and replacement of contracts or entitlement notification to Clearing Members

Market participants would be made aware of events subject to cancellation and replacement of contracts or entitlement notification via a Stock Situation Notice published by the Exchange.

LCH would send cancellation and replacement of contracts or entitlement notification notices to its Clearing Members via the same channels used for LCH's Buying In notices. It would be the responsibility of Clearing Members to bilaterally match settlement instructions resulting from the cancellation and replacement of contracts or entitlement notices in Euroclear Bank under the rules of the Exchange. Clearing Members should make their own arrangements in respect of any obligations they may have with their non Clearing Member customers.

Question 4: What arrangements would Clearing Members put in place to pass on and receive instructions from individual non Clearing Members and how long do Clearing Members believe this development would take?

2.3.4 Settlement of the resulting transactions

The alternative proposal states that the resulting contracts from the process of cancellation and replacement of contracts to Clearing Members would be net transactions with specified Clearing Members as counterparties. It is possible that more than one such net transaction would need to be generated for a Clearing Member in a stock in order to make the process work. These transactions would need to be settled bilaterally between the relevant Clearing Members. The proposal is to generate

net transactions, as this would mean that fewer settlements would be generated. Also, due to the nature of netting, it is not possible to revert to the initial underlying trades.

The process of bilateral settlement would be similar to that referred to in Exchange rules 5232 – 5233, although the Exchange would have to consider developing further rules, as rule 5232 envisages the original trade being returned to the member firms that originally traded; this would not necessarily be the case where the transactions are cancelled and replaced on a net settlement basis.

Question 5a: As it is not possible to revert to the original trade is the proposal to have these settlements as net transactions more or less attractive than the current (default only) process?

Question 5b: Do respondents consider that the additional administrative burden associated with the proposal for bilateral settlement would be significant or of little concern?

2.3.5 Counterparty risk management

Once new replacement contracts are created, settlement of these contracts would no longer be guaranteed by the CCP. In the event of a default of a member firm who is a party to these cancelled and replaced contracts, participants would not be protected by LCH's default rules. Instead, the contracts would be subject to the Exchange's default rules, which stipulate that for non-CCP trades, the Exchange calculates a net sum owed to/from the defaulter based on the difference between the trade price and a hammer price set on the day of default. Participants who are owed money will then claim sums due from the defaulter or its estate in the case of a liquidation or administration.

Once removed from clearing LCH would not be a party to any aspect of the new contracts and Clearing Members would be obliged to accept and settle with the assigned counterparty in all circumstances.

Question 6: Do respondents accept that once the contract has been cancelled and replaced, Clearing Members will be assigned to a Clearing Member counterparty with whom they must settle and LCH would have no further responsibility in the transaction?

2.3.6 Changes to the Exchange's rules

The replacement contracts between Clearing Members would be on-Exchange and be subject to the Exchange's rules. The Exchange would need to develop new rules to accommodate this proposal and the

potentially new obligation on Clearing Members to be responsible for settlement. The current rules can be found at:

<http://www.londonstockexchange.com/traders-and-brokers/rules-regulations/rules-regulations.htm>.

2.3.7 Non FSA authorised member firms and Member Authorised Connection (MAC) customers

The Exchange has a number of member firms that are not authorised by the FSA or any other international regulator. To minimise market risk, these firms (as well as potential MAC customers) are only permitted access to those order books which have a CCP provision. Following the introduction of the CCP for IOB securities, the Exchange granted access to a number of non-authorised firms to the CCP segment of IOB.

The Exchange is currently of the view that, in the event that an IOB security is moved back to the IOBU segment as discussed in section 2.3.2, those member firms should be allowed to trade the security on the IOB order book as they may have entered into positions ahead of the cancellation and replacement of contracts. To exclude them from access to the order book would impact their ability to trade out of those positions.

Question 7: What are the implications (including reference data implications) for trading participants regarding the possibility of settling bilaterally against a non authorised firm? Would this possibility change firms' trading patterns on the IOB?

2.3.8 Charges

In the case of a cancellation and replacement of a contract or entitlement notification to Clearing Members, LCH would charge its Clearing Members with a fee commensurate with its charges for a buy-in notice.

In addition to this standard charge for a cancellation and replacement of a contract or entitlement notification notice, LCH would also recover its development costs in respect of this process during the first two years of operation. The cost recovery fee is based upon project costs divided by the expected cancellation and replacement of contracts or entitlement notification activity in the first two years and applied to all such positions. This would be expected to be set in the region of £125 per contract side.

Clearing Members that settle net would be charged on a per net position, per settlement account basis.

Clearing Members that settle gross would be charged per open position at the time the new product is removed from clearing.

Question 8: Would GCMs look to pass this charge on to their customers?

3 Retrospective dividend record dates

At present, the Exchange will mark in TradElect a depositary receipt as trading ex dividend two days prior to the dividend record date, if notification is received sufficiently in advance to do so.

Notification of the record date is provided to the Exchange from the depositary bank. Delays to this notification may be caused by a number of reasons, including delayed communication from the underlying issuer of the event, or a past date being set as the record date in the underlying market. In most circumstances the depositary bank will align the record date of the depositary receipt with that of the underlying instrument. If the Exchange receives late notification of the record date (i.e. later than 3 business days prior to the record date), the depositary receipt will be marked ex dividend as soon as possible after receipt of notification – normally at the start of the next business day.

It is not possible to mark securities as ex dividend retroactively, as trades in the period between the ex date and the announcement would then be declared ex dividend post trade. To ensure a fair and orderly market the Exchange's priority is to ensure certainty at the point of trade, which would be compromised if ex dates are marked retroactively.

When a security is marked ex dividend late (less than two days prior to record date), buyers in the interim period must claim the dividend back from their seller. This can be a manual and time consuming process. In response to market demand the Exchange has consulted with the relevant depositary banks and proposes to change the procedure for the treatment of late notification of record dates.

Pending the results of this consultation, from 1 August 2009, if notification of the record date has not been received by the Exchange in time to mark the security ex in the normal way (two days prior to record date), depositary banks will be required to set a separate record date which allows appropriate notification to be given to the market. This may mean that the record date of the underlying security is separate from that of the depositary receipt.

In most cases the depositary banks will close the books of the depositary receipt programme from notification of the dividend to the record date on the depositary receipt. Any deposits into the programme during this time would be required to give up any right to the dividend payment.

Payment of the dividend will be made to all depositary receipt holders on the depositary receipt record date. Depositary banks may claim back this

dividend payment from any counterparties who have transferred a holding in the underlying security to the depositary receipt programme between the underlying record date and the books closed date.

This process should reduce or eliminate the impact of late notification of record dates on the IOB, and reduce claims processing required by member firms.

There will be no impact to secondary market trading of the depositary receipt or the underlying during this process. There is also no change to existing LSE rules for member firms. The updated Dividend Procedure Timetable will be available from the date of implementation at:

www.londonstockexchange.com/mainmarket/usefuldocuments

Question 9: Do respondents support this new approach setting ex dates following late notification of record dates? Do respondents have any concerns around the separation of record dates on the underlying and the DR by the depositary banks?

4 IOB market opening hours

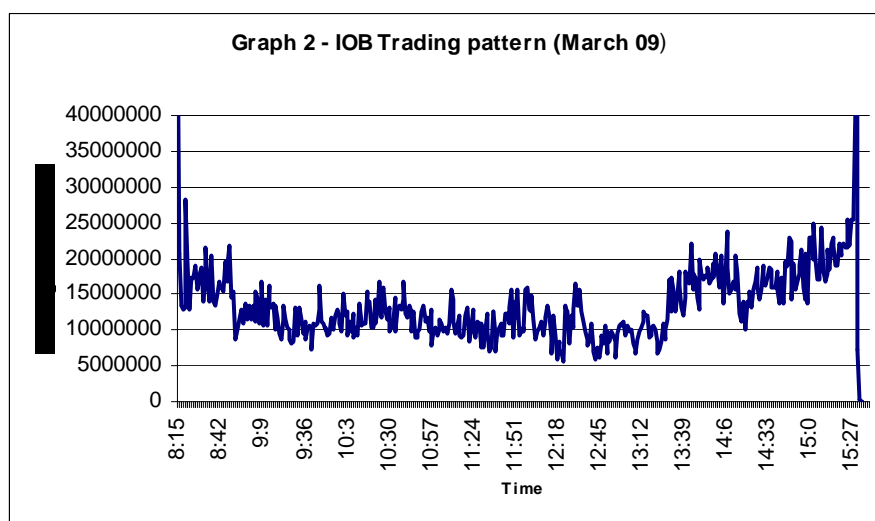
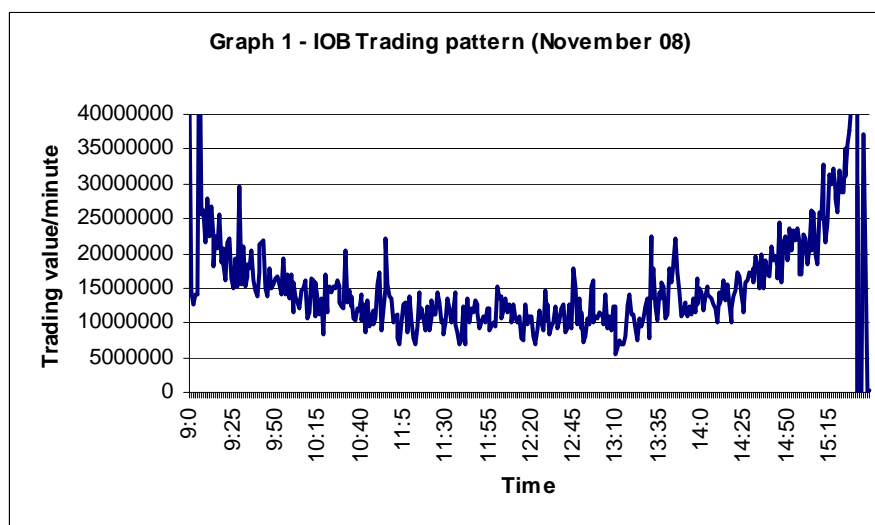
On 23 February 2009, the opening hours for the IOB were changed to align it more closely with the trading hours of key UK, European and Russian markets. The opening auction call now begins at 08:00 London time and continuous trading commences from 08:15.

Trading figures show that participants are making use of the extended trading hours and the change has significantly extended the availability of liquidity on the order book.

- Value traded in the opening auction increased 22% in the month post extension, compared to the month prior to the extension. The value of the FTSE Russia IOB index increased 11% over the same period.
- The number of securities uncrossing at the end of the opening auction has risen 28%, from an average of 15 prior to the extension to an average of 19 post extension.
- The extension has had an impact on the pattern of value being traded throughout the trading day. Post extension, the high value of trading seen directly after the auction lasts for a shorter period, however a slightly higher value is then traded throughout the rest of the trading day (see Graphs 1 & 2)*.

These developments suggest that participants are taking advantage of the additional opportunity to trade in the morning period and may find it easier to locate liquidity at different times in the trading day.

Question 10: Do respondents continue to support the revised opening hours? Is there a requirement for any further revision to either the start or end time of automated trading on IOB? If so what should that revision be?



*Data from November and March was used due to the similarity in values traded during these months. However, these charts are indicative of the broader pre and post extension trading periods.

5 IOB Clearing and overall service

The initial phase of IOB Clearing included the 50 most liquid IOB securities by value traded. The service may be extended to other suitable securities in line with participant demand and in conjunction with LCH.

Changes to the securities included in IOB Clearing will in most cases take place as part of the Exchange's quarterly reviews. Changes will be notified via a Service Announcement and via our Datasync service.

Securities which will be considered for inclusion in the service as part of the September quarterly review are:

- COMMERCIAL INTL.BANK (EGYPT) SAE
- VIMETCO N.V.
- BANK AUDI SAL – AUDI SARADAR GROUP
- BLOM BANK S.A.L.
- RANBAXY LABORATORIES

Question 11: Are there any additional securities that respondents would like to see including in IOB Clearing, or any comments on those suggested above?

Question 12: Do respondents have any feedback on how IOB Clearing is operating since its introduction, specifically in regard to margin levels for IOB business or cost benefits of netting?

Question 13: Do respondents have any other feedback or suggestions in relation to the IOB trading service?

6 Consultation feedback and project implementation

6.1 Consultation feedback

The table below summarises the specific consultation questions regarding market feedback. Please provide responses to these questions and any general feedback on the proposals contained in this document by Wednesday 15 July. All responses should be provided via email to job@londonstockexchange.com.

Should you have any queries or wish to discuss this document or any other aspect of the IOB please contact:

- At the Exchange: Your **Primary Account Manager** or Kara Hyne on +44 (0)20 7797 1608, khyne@londonstockexchange.com
- At LCH: Andrew Rees on +44 (0)20 7426 7469, andrew.rees@lchclearnet.com

| Question no. | Question |
|--------------|----------|
|--------------|----------|

Corporate Actions

| | |
|---|--|
| 1 | <p>Market participants are invited to comment on the proposal set out in sections 2.3.1 to 2.3.8. To be able to elect for options on applicable corporate actions, respondents should understand that under this proposal:</p> <ul style="list-style-type: none">• all of their trades in affected securities will be subject to the cancellation and replacement process, even where the buyer wishes to elect for the default option normally provided by LCH;• they will be exposed to an element of counterparty risk;• they lose a degree of anonymity;• Clearing Members will be responsible for managing the settlement of the trades; and• they will be charged a cancellation and replacement fee, even if they want to accept the default option in an applicable corporate action. <p>Taking into account all of the details of the</p> |
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| | |
|----|---|
| | alternative proposal, would respondents prefer to retain the current service or adopt this proposal? |
| 2 | Do respondents believe that there are other corporate action events that should be included in the proposal and why? |
| 3 | Do respondents believe that all trades should be cancelled and replaced by notification to Clearing Members three days ahead of the last day to participate? If not what period would they suggest and why? |
| 4 | What arrangements would Clearing Members put in place to pass on and receive instructions from individual non Clearing Members and how long do Clearing Members believe this development would take? |
| 5a | As it is not possible to revert to the original trade is the proposal to have these settlements as net transactions more or less attractive than the current (default only) process? |
| 5b | Do respondents consider that the additional administrative burden associated with the proposal for bilateral settlement would be significant or of little concern? |
| 6 | Do respondents accept that once the contract has been cancelled and replaced, Clearing Members will be assigned to a Clearing Member counterparty with whom they must settle and LCH would have no further responsibility in the transaction? |
| 7 | What are the implications (including reference data implications) for trading participants regarding the possibility of settling bilaterally against a non authorised firm? Would this possibility change firms' trading patterns on the IOB? |
| 8 | Would GCMs look to pass this charge on to their customers? |

Retrospective dividend record dates

| | |
|---|---|
| 9 | Do respondents support this new approach to setting ex dates following late notification of record dates? Do respondents have any concerns around the separation of record dates on the underlying and the DR by the depositary banks? |
|---|---|

Opening hours

| | |
|----|--|
| 10 | Do respondents continue to support the revised opening hours? Is there a requirement for any further revision to either the start or end time of automated trading on IOB? If so what should that revision be? |
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IOB Clearing and overall service

| | |
|----|---|
| 11 | Are there any additional securities that respondents would like to see including in IOB Clearing, or any comments on those suggested above? |
| 12 | Do respondents have any feedback on how IOB Clearing is operating since its introduction, specifically in regard to margin levels for IOB business or cost benefits of netting? |
| 13 | Do respondents have any other feedback or suggestions in relation to the IOB trading service? |

6.2 Project implementation

This consultation runs from Wednesday 17 June to Wednesday 15 July.

Following this we will collate all of the responses and aim to publish the results on the Exchange's website at www.londonstockexchange.com/iob.

Any changes to the current procedures will be notified to participants via the Exchange's website and via Service Announcement or Stock Exchange Notice as appropriate.

Sign up to receive Service Announcements at:

<http://www.londonstockexchange.com/information-providers/technical-library/service-announcements/service-announcements.htm>

Sign up to receive Stock Exchange Notices at;

<http://www.londonstockexchange.com/traders-and-brokers/rules-regulations/change-and-updates/stock-exchange-notices/2009/home-2009.htm>



London
Stock Exchange

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