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ALERT MEMORANDUM

FCA Issues First Penalties for Competition Infringements

26 February 2019

On 21 February, the UK Financial Conduct Authority (the "**FCA**") found that Hargreave Hale Ltd ("**Hargreave Hale**"), Newton Investment Management Limited ("**Newton**"), and River and Mercantile Asset Management LLP ("**RAMAM**") had breached competition law by sharing strategic information on a bilateral basis during an initial public offering and a placing, shortly before share prices were set.[1] The FCA imposed fines of £306,300 on Hargreave Hale and £108,600 on RAMAM. Newton was granted immunity and therefore avoided a financial penalty, although its former fund manager, Paul Stephany, was separately fined £32,200 for his role in the breaches.[2] Hargreave Hale is reportedly considering appealing the FCA's decision.

This is the FCA's first competition enforcement decision since it gained competition law enforcement powers on 1 April 2015 and represents the culmination of an investigation that commenced over three years ago. The decision reflects increasing antitrust scrutiny into information exchange in financial markets, provides preliminary insights into the FCA's approach to fines and its investigative procedure in competition cases, and "*demonstrates [the FCA's] commitment to taking enforcement action to protect competition*."

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[1] *See* FCA Press Release of 21 February 2019, "FCA issues its first decision under competition law", available at https://www.fca.org.uk/news/press-releases/fca-issues-its-first-decision-under-competition-law.

[2] This fine was imposed pursuant to the FCA's powers under the Financial Services and Markets Act 2000 rather than its competition powers. *See* FCA Press Release of 5 February 2019, "FCA fines former fund manager Paul Stephany", available at https://www.fca.org.uk/news/press-releases/fca-fines-former-fund-manager-paul-stephany. The FCA's Final Notice against Mr Stephany is available at https://www.fca.org.uk/publication/final-notices/paul-stephany-2019.pdf.

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Background

Although the full text of the competition decision is not yet public, the Final Notice issued to Mr Stephany provides some insight into the underlying facts:

— In July 2015, during the book-building process preceding a placing by Market Tech Holdings Limited, Mr Stephany disclosed the amount and price of the shares he intended to buy to his counterparts at competing fund managers and attempted to persuade them to submit orders at a similarly low price. One of these fund managers subsequently did so.

— In September 2015, during the book-building process preceding the IPO of On The Beach Group plc, Mr Stephany sent two emails to 14 external fund managers at 11 competing firms urging them to consider lowering the price limits on their share orders. Mr Stephany subsequently engaged in follow-up discussions with a number of these fund managers.

Book-building

Book-building is the process through which an underwriter determines the price for shares to be offered in an IPO or placing, based on demand from institutional investors. The underwriter will build a "book" by accepting orders from institutional investors, who will in turn indicate the number of shares they would be prepared to buy and the price they are willing to pay. The final price will be set by reference to the volume of orders and the price range offered. The book-building process is intended to result in a fair price which reflects genuine market demand. In its Final Notice, the FCA suggested that although there may be circumstances in which it is legitimate for competing investors to discuss certain aspects of their bids, they should not use, or attempt to use, their collective power to undermine the proper price formation process. The full text of the competition decision should provide further guidance in this respect.

The FCA found that each of Newton, Hargreave Hale, and RAMAM had "*disclosed and/or accepted otherwise confidential bidding intentions, in the form of the price they were willing to pay and sometimes the volume they wished to acquire. This allowed one firm to know another's plans during the IPO or placing process when they should have been competing for shares*."

The FCA noted that such conduct could undermine the process by which prices were set and result in a reduction in the share price achieved by an IPO or placing. This could in turn increase a company's costs of raising capital and financing investments. The FCA made this statement in general terms, without any indication as to whether it had made any specific findings to this effect in the present case.

Analysis

The FCA's decision provides a number of important insights into its approach to competition enforcement, including with respect to the types of infringement it is willing to pursue and its investigative procedure. It also reflects continued global antitrust scrutiny into co-operation in financial markets.

Increased focus on information exchange

The FCA's decision demonstrates an increasing readiness to scrutinise information exchanges between financial institutions under competition law, even if such exchanges are not accompanied by any explicit agreement to fix prices, occur on a bilateral basis, and do not appear to form part of any wider pattern of inappropriate conduct.

Although the European Commission ("**EC**") imposed significant fines on various financial institutions for anti-competitive information exchange in its benchmark-related investigations, it appears to have analysed these exchanges as "secondary" infringements, underpinning a "primary" infringement consisting of an agreement to fix prices. The UK's Office of Fair Trading ("**OFT**") took a broader approach in its 2011 decision on the disclosure of competitively sensitive information by RBS to Barclays, relying on a presumption that Barclays had taken the information received from RBS into account in pricing its future

deals.[3] But in each case, the exchanges formed part of a wider pattern of conduct which took place more regularly over months, if not years.

The FCA's decision to base its first competition enforcement decision on a small number of instances of bilateral information exchange suggests that it may be prepared to apply a relatively low threshold to the types of conduct it is prepared to investigate and sanction under its formal competition enforcement powers. Financial institutions will need to adapt their compliance programmes and revisit their risk appetites accordingly – in particular if they are subject to the notification requirement in Principle 11 of the FCA's Handbook, which requires regulated firms to notify the FCA if they have or may have committed a significant infringement of any applicable competition law.[4]

Competition for corporate control rather than products/services

In light of the FCA's objective to promote competition in the interests of consumers, it is perhaps surprising that its first competition enforcement decision relates to a wholesale rather than retail activity – the sale/purchase of corporate control (*i.e.*, shares) rather than products or services. While agencies and courts in the United States and Australia have shown some interest in pursuing antitrust enforcement in this area, this has not historically been the case in the EU.[5] Having said that, this decision builds on the FCA's work in wholesale markets (as evidenced by its market studies) and may lead to further scrutiny of such arrangements across the EU.

FCA enforcement procedure

According to press reports, the FCA commenced its investigation in late 2015 or early 2016, shortly after it acquired competition enforcement powers. It announced the issue of a Statement of Objections ("**SO**") on 29 November 2017, nearly 15 months ago.[6] Although there are a number of important procedural steps that need to take place after the issue of an SO and before a final decision can be taken (*e.g.*, providing the companies under investigation with access to the case file and an opportunity to make both written and oral submissions), the time lag between the two steps in this case was significant. By way of comparison, the UK's primary competition authority, the Competition and Markets Authority ("**CMA**"), has on average taken five months from SO to final decision in the Competition Act 1998 cases launched since it was established.[7] The delay in this case may be attributable to the fact that this is the FCA's first

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[3] Hargreave Hale has questioned the application of the RBS/Barclays presumption to its own conduct, claiming that the FCA made "*a number of legal and factual errors*" in its analysis, including by holding Hargreave Hale liable for receiving information on an unsolicited basis, without altering its own bidding behaviour as a result. *See* "Hargreave Hale disputes FCA competition breach decision", Portfolio Adviser, 21 February 2019, available at https://portfolio-adviser.com/hargreave-hale-disputes-fca-competition-breach-decision/.

[4] *See* FCA Handbook SUP 15.3.32, available at https://www.handbook.fca.org.uk/handbook/SUP/15/3.html.

[5] Typically in relation to consortium bidding by private equity firms to purchase a particular company. In October 2006, the Antitrust Division of the United States Department of Justice launched an investigation into whether the largest private equity firms had colluded to keep buyout prices down. Although this investigation was ultimately closed without further action, a group of shareholders was awarded US$590.5m in a series of related settlements in February 2015. In March 2013, the Australian Federal Court awarded Norcast (the owner of the relevant target) US$22.4m in damages for bid-rigging by Bradken, which had agreed that a third party (Castle Harlan) would buy the target at a reduced price, and then sell it on to Bradken.

[6] *See* FCA Press Release of 29 November 2017, "FCA issues first statement of objections to four asset management firms", available at https://www.fca.org.uk/news/press-releases/fca-issues-first-statement-objections-four-asset-management-firms. The SO was also issued to a fourth asset management firm, Artemis Investment Management LLP ("**Artemis**"), but the FCA decided that there were no grounds for action in respect of conduct between Artemis and Newton that took place between April and May 2014 in relation to an IPO.

[7] The range is, however, significant (from 16 days in the 2016 investigation into online sales of posters and frames to nearly 15 months in the 2015-2016 investigation into anti-competitive practices in the sports equipment sector).

decision under its competition law powers. The overall length of the investigation is also comparable to the duration that might be expected in a non-competition FCA enforcement case.

Through its enforcement action against Mr Stephany, the FCA has indicated a readiness to apply its financial regulatory powers alongside its competition powers where appropriate. This is consistent with the FCA's increasing focus on holding senior management to account (although Mr Stephany was not a senior manager, he was an "*experienced industry professional*"). Individuals involved in future FCA competition investigations should be alive to the risk that the FCA may choose to pursue them separately (and even in circumstances in which the company for which they work(ed) has been granted immunity).

Continued antitrust scrutiny into co-operation between financial institutions

The FCA's decision reflects continued scrutiny from competition authorities around the world into the boundaries between appropriate and illegal co-operation between financial institutions. By way of example:

— The EC is currently conducting at least four separate cartel investigations in the financial sector, based on alleged co-ordination and inappropriate information exchange in the setting of foreign exchange rates and the trading of foreign exchange options, European government bonds, and US Dollar supra-sovereign, sovereign, and agency bonds.

— The EC has commissioned a study on the operation of syndicated lending in the EU and its "*possible implications for competition policy*", following observations that such lending involves "*close cooperation between market participants in opaque or in-transparent settings, such as over-the-counter activities, which are particularly vulnerable to anti-competitive conduct*."[8] The results of the study are expected in early 2019 and will follow competition enforcement by EU Member States in this area.[9]

— In June 2018, the Australian Competition and Consumer Commission announced that it had brought criminal cartel charges against an issuer and a number of underwriting banks for allegedly co-ordinating on the price and timing for selling the shares remaining following the issuer's placing.[10]

These developments indicate increasing readiness on the part of competition authorities to tackle the difficult task of distinguishing between permissible and anti-competitive conduct in circumstances in which financial institutions act as both counterparties and competitors and a certain degree of co-operation is necessary for the markets to function. Although the final decisions in these investigations should provide useful guidance on where to draw the line,

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[8] *See* European Commission DG Competition Management Plan 2017, page 11, available at https://ec.europa.eu/info/sites/info/files/file_import/management-plan-comp-2017_en_0.pdf. *See also* associated tender notice at https://ted.europa.eu/udl?uri=TED:NOTICE:133880-2017:TEXT:EN:HTML.

[9] Including in Spain, the UK, and the Netherlands. In February 2018, the Spanish Markets and Competition Commission fined four Spanish banks €91m for colluding to fix the prices of interest rate derivatives attached to syndicated loans (*see* https://www.cnmc.es/sites/default/files/1928672_17.pdf). In February 2017, the FCA announced that it had issued a number of "on notice" letters to firms in relation to the disclosure or exchange of competitively sensitive information relating to the terms and conditions of syndicated lending (*see* FCA Regulation Round-up February 2017, available at https://www.fca.org.uk/publication/documents/rru-february-2017.pdf). In 2010, the Netherlands Competition Authority noted that the number of banks offering syndicated loans had decreased and that the area could be vulnerable to anti-competitive conduct, although it did not find any infringement (*see* "NMa: limited choice for undertakings when seeking syndicated loans", available at https://www.acm.nl/en/publications/publication/6254/NMa-limited-choice-for-undertakings-when-seeking-syndicated-loans).

[10] *See* Australian Competition and Consumer Commission Press Release of 5 June 2018, available at https://www.accc.gov.au/media-release/criminal-cartel-charges-laid-against-anz-citigroup-and-deutsche-bank.

until then, financial institutions should exercise particular caution in any dealings with competitors.

What's next?

The FCA's decision represents an important step in its evolution as a concurrent competition authority. Although the fines imposed are relatively low (representing less than 1% of each company's turnover), the FCA appears to have shown a willingness to take enforcement action in relation to conduct that has not previously been sanctioned on a standalone basis by the UK and EU competition authorities. Whether this will continue in light of the expected increase in the FCA's workload post-Brexit remains to be seen. If, as the CMA has suggested, the UK authorities pursue the "*big cartels in the financial sector*" that were previously within the exclusive jurisdiction of the EC, we may see more wide-ranging investigations and far more significant penalties in the future.

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