Beware of cartel practices

As regulatory reforms gather momentum in the EU, financial services face increased competition compliance risks

REGULATORS ACROSS EUROPE are increasing their pressure on the financial services sector, with the news a few months ago that the UK Financial Conduct Authority (FCA) is poised to launch a review of the wholesale financial markets sector. According to the FCA, the sector plays a "crucial role in the economy and it is important that it is not only clean but also competitive". Already, the FCA has looked at or is looking at retirement incomes, cash savings, insurance add-ons and SME banking using its existing competition powers.

The financial services sector is one of the more heavily regulated industries in Europe, but as recent history shows, there is widespread political and regulatory appetite to put in place measures that can avoid a repeat of the 2008 crisis. In its wake, UK authorities handed responsibility "to promote effective competition in the interests of consumers in the markets for regulated financial services" to the FCA. From April 2015, the watchdog will gain the power to enforce competition law, in addition to its existing regulatory regime. In addition, the UK has a new competition authority, the Competition and Markets Authority (CMA), which is keen to show its strength and effectiveness.

Internationally, there are a range of initiatives to improve the supervision of global financial services markets, with the European Commission setting out its vision in its report, *A reformed financial sector for Europe*, launched in May. Although politicians may agree further reform is required, completion of the project is still some way off.

In the meantime, regulatory reform continues within individual EU states.

For financial services organisations active in the UK market, greater competition compliance vigilance is required by, for example, carrying out regular competition audits and training. The FCA has already undertaken a number of market studies to review whether the markets in question are working well for consumers. The FCA can then, under current powers, request the CMA to consider a financial services market in depth and whether this comprises features restricting competition. Alternatively, the FCA can take regulatory action under its general remedial powers.

From next year, the FCA will also have powers to require the CMA to investigate a financial services market in depth. Additionally, it will also be able to investigate suspected breaches of the UK or EU rules prohibiting cartels and other anti-competitive arrangements between competitors and abusive conduct by dominant players. Furthermore, the FCA will also be required to consider whether it would be more appropriate to use its powers under competition law, before using its regulatory powers.

The FCA has not been slow to use its existing powers, as illustrated by the call for inputs to the wholesale securities and investment markets, as well as related activities, such as corporate banking. This process closed in October and the FCA is expected to decide in a few months which areas will merit closer attention through a market study.

Investigatory powers

Competition law issues that can trigger regulatory intervention can take a range of forms. For example, if the market appears not to be offering choice or value for money to consumers or market entry by new players is difficult, then a market study and, potentially, a full market investigation may follow. Where more specific conduct is suspected, such as information sharing, price fixing, market sharing among competitors or abusive conduct by a dominant company, the authorities can investigate and impose fines of up to 10% of worldwide turnover.

A market investigation is an in-depth investigation into the operation of a market, has significant consequences for any business that has come under the spotlight. The authorities have extensive powers to require the provision of evidence and data and, at the end of the process, to impose remedies.

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Such investigatory powers – which if unlawfully resisted, can lead to significant penalties – include the ability to require individuals to give evidence, provide specific documents or categories of documents and to demand that businesses supply a wide range of data and information.

Following an investigation, remedies to address competition issues can include the need to divest parts or assets of businesses, measures to reduce switching costs, a change in behaviour, such as directing companies to cap prices or give clearer notice of price changes or recommending legislators take actions to change industry regulations.

Although a market investigation is not normally triggered by a specific concern about conduct infringing the prohibitions described below, a substantial risk arises that in the course of a data trawl, any anti-competitive conduct that has occurred may come to light. It is, therefore, very important to ensure full compliance with the rules prohibiting anti-competitive conduct among competitors or by dominant players if subject to a market investigation. Otherwise, a further investigation could be on the cards.


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Most business people will know that price-fixing and market sharing among competitors is illegal. However, what is often not appreciated is that informal arrangements, such as exchanges of information, could be regarded as having similar effects to a cartel, even if there is no agreement as such. This is where many businesses fall foul of the law. As illustrated by an earlier UK case involving former banking colleagues, now working for competing institutions, a conversation over a beer can prove costly. Casual chats took place between the individuals at various social, client and industry events and, through these exchanges, staff at one bank communicated to staff at another bank an intended pricing strategy for professional loan products. The information was subsequently discussed within one of the other banks, which led the competition regulator to conclude that the conduct amounted to an agreement and/or concerted practice, which was intended to restrict competition in the supply of professional loan products.

Although one of the banks escaped a fine by co-operating with the authorities, the other was fined more than £28m (€35m).

Across many international jurisdictions, the concept of leniency is well established. In the UK, organisations may see fines reduced or waived in return for taking information to the authorities and co-operating with any subsequent investigation. A nil fine, however, is available only to the first leniency applicant to reach the CMA or European Commission. If anti-competitive conduct comes to light, therefore, it is essential to act promptly. Delay may mean that a competitor gets in first and obtains the prize of a nil fine.

Competition compliance – top tips

- All businesses, of any size, large and small, should have a compliance programme.
- Competition policy: an integral part of the compliance programme, the policy should be clear and succinct, so that risks can be identified and assessed.
- Monitoring: ensure compliance with the law. This should include a mechanism for reporting competitor contacts. Relevant staff needs to confirm on an annual or other regular basis that they have complied with it.
- Training: a tailored approach is essential.
- Dawn raids: check and review whether existing procedures should be revamped, particularly in light of the authorities' new increased powers.

Businesses with high market shares need to be aware of the risk of abusing their dominance by unfair practices such as refusing access to key inputs necessary for competitors or rebates designed to achieve loyalty or predatory, that is, unfairly low, pricing designed to drive competitors out of the market. This does not concern only the giants of this world, such as Google or Microsoft and these rules can apply to much smaller businesses in niche markets that may be difficult, for one reason or another, to enter.

For example, spare parts for a product are often regarded as a separate market from the product itself, so a manufacturer can often be dominant in its own spare parts. Fines for breach of these rules, in the UK, other EU countries or across more than one EU member state, can be up to 10% of group worldwide turnover. Even at the UK level, fines of tens of millions are common, and following an EU investigation, hundreds of millions are not unheard of. For instance, in the recent Libor/Euribor investigation, fines totalling €1.7bn have been imposed on a number of banks, with possible further fines still anticipated.

An ongoing process

For individuals, the risk is also increased of committing a criminal cartel offence, since the law was broadened in scope earlier in the year to make it easier for the authorities to prosecute individuals in the criminal courts for cartel activity.

The existing risks associated with anti-competitive conduct already are set to increase further next year and businesses in the financial services sector need to think now about competition compliance. The FCA, with its already substantial powers and significant resources, may well be able to spot suspect conduct and deal with it under competition powers. Most importantly, perhaps, when responding to a call for inputs or other preliminary, informal investigation, financial services businesses must be aware of the significant powers that can be brought to bear should they disclose too much or inadvertently draw attention to something that suggests anti-competitive conduct.

Financial services firms should start with a risk assessment: do they/their people understand what conduct is likely to be regarded as anti-competitive? Who within the business could be at risk of infringing competition law and have they received training?

Crucially, knowing how business is conducted in practice enables the correct questions to be asked so that any concerns are brought to light. Only then can such practices be ended and, if the conduct is serious, a leniency application considered. It may be necessary to take some 'deep dives' into internal emails and interview staff to understand the nature and scope of the concerns that come to light. It should be remembered that compliance is, however, not a one off but an ongoing process that needs to be kept fresh and relevant to be effective.

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