SLAUGHTER AND MAY

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European Commission publishes report on EU loan syndication and its impact on competition in credit markets

On 5 April the European Commission published a **report** it had commissioned on "EU loan syndication and its impact on competition in credit markets".

Loan syndication occurs where several lenders work together to provide portions of a loan, which would be too large and risky for a single bank. The study focused on loan syndication in the UK, France, Germany, the Netherlands, Poland and Spain, as the most significant countries in terms of location of borrowers, lenders and investors. The market segments covered by the report are Leveraged Buy-Outs (LBOs), Project Finance and Infrastructure (PF/INFRA).

The report suggests that there are few areas where loan syndication processes in themselves could represent a risk to competition law. However, it does identify some features of the syndication process that could lead to anti-competitive outcomes, although the authors consider these risks to be low in most cases.

Competitive bidding process for appointing the lead banking group

The report considers whether (generic or deal-specific) market soundings between banks could give rise to competition concerns. The report found that there is a risk that soundings between Mandated Lead Arrangers (MLAs) and investors could be communicated back to origination desks, and that this risk is exacerbated where there is no functional separation between syndication and origination desks. Where soundings (even generic soundings) take place with other MLAs, there is a risk that the process could be abused so as to facilitate collusion, although the report recognised that there is a relatively low likelihood of this occurring in the LBO segment. The risk of collusion occurring is mitigated to some extent by the use of NDAs during the bidding process, which help to put lenders "on clear notice" of the borrower's expectations, even if NDAs are difficult to enforce in practice.

In relation to PF/INFRA loans, the report suggests that there is a heightened risk that interactions between lenders could cross over from generic to deal-specific market soundings during the bidding stage, thereby increasing the risk of competition concerns arising. The report also highlights the risk that the use of a single MLA (which is more likely to occur for PF/INFRA loans) could lead to

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coordination between syndicate members such that "*the price and terms of the loan move against the borrower*".

Post-mandate to loan agreement

The report finds that the scope for lenders discussing loan terms so as to move against the borrower at the post-mandate stage is low. In both LBO and PF/INFRA segments, the loan terms are agreed bilaterally between the borrower and each lender, with joint discussions between lenders generally limited to agreeing documentation and syndication strategy.

However, in relation to PF/INFRA loans, the borrower might bring lenders together at an earlier stage of negotiations to discuss loan terms (e.g. in the context of a club deal). Monitoring of these discussions is important in order to manage the risk of collusion, particularly for comparatively less sophisticated borrowers.

More generally, the report finds that there is a "definite risk" that lenders can observe each other's behaviours and strategies during multiple interactions, which could allow them to engage in coordination on future transactions. However, the authors did not find any evidence that this happens in practice and the risk is regarded as relatively low.

"Moderate concern" in relation to bundling of ancillary services

One area flagged as being of "moderate concern" is the practice of bundling the sale of ancillary services with the loan agreement. The report advises that the sale of ancillary services be kept separate from the syndication processes where services are not directly related to the loan, noting that the **Financial Conduct Authority** has banned similar types of arrangements in the UK. These practices have received recent scrutiny by competition authorities. In February 2018 the Spanish Markets and Competition Commission fined four Spanish banks €91 million for allegedly conspiring to offer interest-rate derivatives attached to syndicated loans under conditions other than those agreed with customers.

Using debt advisers

The use of advisers who are also part of the syndicate is widespread among borrowers and sponsors. The report finds that where a lending bank is providing an advisory role, this is normally functionally separate from the lending role and adherence to protocols should prevent the risk of the borrower not having an independent adviser. The report noted that concerns might arise where the advising bank influences the borrower towards a strategy or debt structure that suited its lending arm. However, the authors found that the lenders' internal protocols are generally constituted to prevent this from happening.

Coordination by lenders on the sale of the loan on the secondary market

The report found no evidence of coordinated activity to manipulate prices on the secondary market. The sophisticated nature of the participants in the secondary market was considered sufficient to limit any attempt by sellers to manipulate debt prices. The report observes, however, that borrower restrictions on secondary trading limit the development and efficiency of secondary markets, which could have (minor) knock-on effects for primary markets, particularly in the PF/INFRA segment.

Refinancing in conditions of default

The report notes that collaborative discussions among syndicate members in connection with a potential restructuring may be efficiency enhancing, but could also increase the risk of banks acting in a coordinated manner. However, these discussions are generally not undertaken by teams involved in loan origination and the existence of competition policies and training can help to address the risk of collusion. The report finds that potential involvement of lenders from outside the syndicate may act as a limit on the bargaining power of the existing syndicate members.

Ensuring competitive outcomes

The report highlights the importance of certain safeguards to ensure competitive outcomes during the syndication process.

- MLAs should maintain adequate training programmes and policies, in particular concerning the management of conflicts of interest and the duty of care owed to clients. MLAs should also ensure that loan pricing and terms are not adjusted upwards to a highest common denominator until other options (such as approaching additional lenders or restructuring the loan) have been exhausted.
- Banks should take steps to avoid unwarranted information exchange between origination and syndication desks, which might otherwise lead to anti-competitive alignment between banks on pricing.
- While ancillary services not directly related to the loan can be used as part of the loan negotiation, it is advisable for syndicates to limit cross-sale of ancillary services to avoid the risk of impairing competitive conditions.

At this stage, the Commission has not responded to the report's findings or indicated whether it is minded to open its own sector inquiry. While the report's findings do not necessarily signal an increased risk of imminent enforcement activity in this area, the syndicated lending market, and financial services more generally, are expected to continue to attract scrutiny from the Commission and national authorities.

Other developments

Merger control

European Commission continues clampdown on procedural breaches with €52 million fine for General Electric

On 8 April 2019 the Commission **announced** that it had fined General Electric €52 million for providing incorrect information during the Commission's investigation of GE's proposed acquisition of LM Wind. This is the second Commission fine for provision of incorrect or misleading information under the 2004 EU Merger Regulation (EUMR), following Facebook's €110 million fine in May 2017 in relation to the Commission's 2014 investigation of the WhatsApp acquisition.

In its 11 January 2017 notification, GE stated that it did not have wind turbines for offshore applications in development with a higher power output than its existing 6 megawatt turbine. However, the Commission learnt through a third party that GE was offering a 12 megawatt offshore wind turbine to potential customers. GE therefore withdrew its notification on 2 February 2017, and re-notified on 13 February 2017, this time including complete information on high power developments. The Commission approved the acquisition on 20 March 2017.

The Commission considered that the infringement was serious because it prevented the Commission from having all relevant information for the assessment of the transaction. The Commission also considered that GE, with whom it had contact on the subject of pipeline products in the relevant market, should have been aware of its legal obligations and of the relevance of the information. However, the Commission described the breach as a negligent provision of incorrect information, rather than as a provision of "incorrect and misleading" information that was "at least negligent", **as it had with Facebook**, perhaps explaining the smaller size of the fine. The Commission's investigation into whether the parties to the Merck and Sigma-Aldrich merger provided incorrect or misleading information is ongoing.

Antitrust

ACCC drops antitrust probe against "Big Four" consulting firms

On 4 April 2019 it was **reported** that the Australian Competition and Consumer Commission (ACCC) dropped its preliminary investigation into the Australian audit and consulting businesses of the Big Four accountancy firms (Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers).

The investigation reportedly commenced following a written request in September 2018 from parliamentarians of the Australian Labor Party about allegations of anti-competitive behaviour. In conducting its investigation, the ACCC, amongst others, requested information about engagement letters, draft proposals and notes about the Big Four's public sector work. The ACCC concluded that it had not found sufficient evidence to warrant further investigative action.

The wider audit sector is currently under investigation in the UK. The UK's Competition and Markets Authority is conducting a market study on the sector, due to finish by October 2019, and the UK Parliament's Business, Energy and Industrial Strategy Committee recently released a **report** setting out its recommendations for the industry.

General competition

European Commission publishes report on competition policy for the digital era

On 4 April 2019 the Commission published a **report** on "Competition policy for the digital era", authored by three specialist advisers. The report focuses on three key features of the digital economy: (i) extreme returns to scale, (ii) network effects and (iii) the key role of data. According to the report, these features lead to the creation of digital ecosystems and give incumbents a "strong competitive advantage". While the report concludes that the basic framework of competition law continues to provide "*a sound and*

sufficiently flexible basis for protecting competition in the digital era", certain concepts, doctrines and methodologies must be adapted and refined. Its recommendations and suggestions include:

- **Goals and methodologies of EU competition law**: the timeframe and standard of proof should be rethought due to the fast pace of digital change; insisting that harm be identified with a high degree of probability would result in under-enforcement. Authorities should also "*put less emphasis on analysis of market definition, and more emphasis on theories of harm and identification of anti-competitive strategies*". The assessment of market power has to be case-specific and take account of insights drawn from behavioural economics.
- **Platforms**: it is essential to protect competition both "for" the market and on the platform (which in many cases might be the same as protecting competition "in" the market). While a case-by-case analysis is always required, strict scrutiny is therefore appropriate, for example, in relation to Most Favoured Nation or best price clauses. It is also key to ensure that multi-homing and switching are possible.
- **Data**: the significance of data and data access for competition will "*always depend on an analysis of the specificities of a given market, the type of data, and data usage in a given case*". For example, where competitors request access to (non-personal) data from a dominant firm, an in-depth analysis will be required as to whether such access is truly indispensable to compete.
- **M&A**: it is too early to change the EUMR's jurisdictional thresholds in response to concerns that these thresholds are insufficient to "catch" acquisitions by dominant platforms of small start-ups with a quickly growing user base and significant competitive potential (but low turnover). Instead, authorities should monitor the performance of the value-based thresholds that some EU Member States have introduced and the functioning of the EUMR referral system.

EU Commissioner Vestager has welcomed the report indicating that the Commission will need to take some time to consider the report's suggestions before reaching any firm conclusions about next steps. However, in her view, the most important message from the report is "rather simple": the Commission must ensure it keeps up with the constantly changing markets because "*a strong European economy needs effective competition, to keep it innovative and dynamic and successful*".

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