Competition at the Financial Conduct Authority

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Introduction

This article describes the Financial Conduct Authority's (FCA's) competition mandate and concurrent powers, how it has set itself up to exercise and pursue that mandate and exercise those powers, and the competition work it has undertaken so far and that it anticipates undertaking in the medium term.

FCA's competition mandate under the Financial Services and Markets Act 2000

The FCA's competition mandate was introduced as part of the reform of the financial regulatory authorities following the financial crisis of 2008. The Independent Commission on Banking found that:

> 'One of the reasons for long-standing problems of competition and consumer choice in banking and financial services more generally has been that competition has not been central to financial regulation. The current reform of the financial regulatory authorities, especially the creation of the FCA, presents an opportunity to change this, which in the Commission's view should be seized.'[2]

In light of this, the FCA has been given a mandate to promote competition, to be found in the early sections of the Financial Services and Markets Act 2000 (FSMA). Its s 1B(1) provides that the FCA must act in a way which is compatible with its strategic objective and advances one or more of its three operational objectives.

The strategic objective is to ensure that the relevant markets function 'well' (FSMA, s 1B(2)). Those markets are the financial markets, regulated financial services, and services provided by non-authorised individuals carrying out regulated activities without breaking the FCA's rules (s 1F).

The three operational objectives are consumer protection, integrity and competition (s 1B(3)).[3] Additionally, the FCA has a competition duty, in that, so far as is compatible with acting in a way which advances the consumer protection objective or integrity objective, it must discharge its general functions in a way which promotes effective competition in the interests of consumers (s 1B(4)).[4]

To date, the competition mandate has been most visible in the market studies carried out by the FCA, but it is also reflected in its other work, such as Project Innovate, and internal FCA activities, grouped together below under the heading 'embedding competition'. We describe each in turn next.

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1 The authors are a Director, Manager, and Technical Specialist respectively within the FCA's Competition Division. While we are grateful for comments received from FCA colleagues and the CMA, any views are personal and errors our responsibility.

2 Final Report and Recommendations of the Independent Commission on Banking, p 17 and para 6.20.

3 The competition objective applies to the markets are for regulated financial services and recognised investment exchanges (FSMA, s 1E(1)).

4 The general functions are defined in FSMA, s 1B(6): broadly, rule-making, preparing and issuing codes, giving general guidance and determining the FCA's general policy and principles.

Market studies

There is no free-standing 'market studies' power in FSMA. Rather, the FCA has used its existing FSMA powers in pursuit of its competition mandate in order to review certain markets in a holistic way, in order to assess whether a specific market is working well for consumers. Such studies are not necessarily limited to a competition assessment: they may also look for issues of consumer protection and/or market integrity.

Interventions at market level mean that the FCA can respond comprehensively to issues and promote competition in the interest of consumers, while also addressing the potential effects of poor conduct on consumers and other firms in a sector. The FCA can also address specific issues within firms. The FCA sees market studies as an effective and powerful way of identifying and mitigating problems and addressing these across a large number of firms, which in turn can benefit a large number of consumers. If firms in a market are subject to strong competitive pressures, there may be less need for individual assessments.

Since 2013, the FCA has completed market studies into general insurance add-ons, cash savings and retirement income, and a review of competition in the wholesale sector to gather views on areas that might benefit from further investigation. Currently there are market studies underway into credit cards and into investment and corporate banking services.[5] The FCA has also undertaken shorter pieces of work such as a review of the current account switching service.[6]

The FCA also undertakes 'thematic reviews'. These are based on the same set of FSMA powers as its FSMA market studies, but typically tend to consider a more focused issue or specific regulation, rather than a market as a whole. However, there is no bright line between market studies and thematic reviews. At the end of 2014, the FCA announced a strategic review with some organisational changes.[7] These brought together within the Competition Division more of its market-based work (ie cross-market thematic work and market study work) aiming to look broadly across regulated sectors and products.

Following a market study (or thematic review), the FCA can use its FSMA tools to address any issues identified. As noted, these can be market-wide, such as making rules and issuing general guidance to firms; or firm-specific, such as interventions to cancel or vary a firm's permissions or requirements and disciplining firms for failure to comply with requirements. There are consultation obligations for most market-wide remedies. To state the obvious, these FSMA remedy powers can only apply within the regulatory perimeter, that is to regulated firms, approved persons and certain others such as investment exchanges and payment service providers that fall within the FCA's remit.

Project Innovate

Project Innovate is an FCA initiative to help firms looking to introduce innovative financial products and services to the market.[8] It has a dedicated team that helps eligible firms through the authorisation process necessary to enter a regulated market, and subsequently for up to a year. More generally, the FCA is also seeking to add more flexibility to its regulatory framework and remove barriers to entry. Project Innovate helps the FCA identify where parts of the regulatory framework may be impeding market development. The aim is to encourage innovation without eroding consumer protection or the integrity of the financial system in the UK.

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5 See www.fca.org.uk/news/list?ttypes=Market+study&yyear=&ssearch=.
6 See www.fca.org.uk/about/what/promoting-competition/current-account-switch.
7 See www.fca.org.uk/static/documents/reports/fca-our-strategy-december-2014.pdf.
8 See https://innovate.fca.org.uk.

This appears to be a novel role for a regulatory or competition authority, which typically aims to identify and remedy specific competition issues, rather than actively foster competition by assisting new entrants on a continuing basis.[9]

Embedding competition

As well as its use of tools to promote competition or address specific competition issues, the FCA is working to embed competition considerations across the range of FCA work. This may be less visible but is a key part of its competition work. This includes, for example, ensuring that it assesses what the impact on barriers to entry and expansion may be when developing policy and new rules.

One example is the consultation on the possible introduction of a FRAND (Fair, Reasonable, and Non-Discriminatory) pricing obligation on the administrators of regulated benchmarks.[10] Following the financial crisis and increased scrutiny,[11] benchmark administrators are subject to increased regulation to ensure their integrity and credibility. However, the FCA is now aiming to ensure that they cannot use the market power they may have for anti-competitive purposes, such as excessive or discriminatory pricing, or margin-squeezing downstream rivals.

Much of the regulatory framework within which firms in the UK operate is set by European legislation and/or was put in place in the days of the Financial Services Authority, prior to the current competition mandate of the FCA. As well as looking at new policies as they develop, the FCA has considered the effect of the existing Handbook on competition. Firms and their advisers can assist the FCA by drawing to its attention any specific provisions that have an impact on competition that is disproportionate to their intended aim.

The FCA's concurrent competition powers

The powers

On 1 April 2015, the FCA obtained concurrent powers with regard to the provision of financial services. This means that it now has the powers to enforce the Chapter 1 and 2 prohibitions of the Competition Act 1998 (CA98)[12] and Arts 101 and 102 of the Treaty on the Functioning of the European Union (TFEU),[13] undertake market studies under the Enterprise Act 2002 (EA02) and make market investigation references to the CMA under EA02.[14]

The powers are concurrent, in that the CMA can also exercise them with regard to financial services – although only one authority can exercise the functions for a given case at any one time. The term 'financial services' is not defined, but it extends beyond firms, persons and services regulated by the FCA under FSMA.

These powers are independent of but consistent with the FCA's FSMA powers. In particular, s 234N provides that the FCA's general duties do not apply to the FCA when carrying out its concurrent functions. Equally, s 1B provides that the strategic and operational objectives only apply when the FCA is discharging its general functions, which do not include its concurrent functions.

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9 Merger or market investigation remedies may entail divestment or other structural or quasi-structural interventions, designed to make a market structure more competitive by strengthening a specific undertaking, which might be a new entrant.

10 See www.fca.org.uk/news/cp15–18-frand-access-benchmarks.

11 See www.gov.uk/government/uploads/system/uploads/attachment_data/file/191762/wheatley_review_libor_finalreport_280912.pdf.

12 FSMA, s 234J(2)(a), (b).

13 FSMA, s 234J(2)(c), (d).

14 FSMA, s 234I(2).

These new powers mean that the FCA has joined the familiar list of established concurrent regulators, such as Ofgem, Ofcom, etc. It had been out of line with other such regulators, who not only have objectives to promote competition but also have the specific enforcement tools to tackle those competition failures brought about by firms' behaviour. It is worth noting, however, that the FCA is a conduct regulator, rather than an economic regulator. This makes the FCA somewhat different to other concurrent regulators, whose competition mandate is based on regulating former nationalised monopolies.

Government agreed that equipping the FCA with a greater range of powers would enhance its credibility when engaging with firms. Gaining concurrent competition powers has also put the FCA in a better position to engage at a European level to address cross-border competition issues effectively.

This should allow the FCA to bring its financial services expertise to bear in enforcing the CA98 and TFEU competition prohibitions. As noted, the concurrent powers are not limited to regulated activities/ authorised persons, but extend to 'financial services' more broadly. Under FSMA, s 234O, the Treasury is the arbiter of whether the FCA's concurrent powers apply to any given situation. Ultimately, if there is doubt, the CMA will always have the power to act.

Concurrency in practice

UK financial services have long been subject to competition law (since 1958, in terms of the European law prohibitions originally contained in the EEC Treaty, and since 2000, in terms of CA98). This means that the principal change is institutional, ie, who can enforce against suspected breaches rather than which conduct is prohibited. Given the variety of potential enforcers, arrangements are in place to ensure that only one authority acts at any one time. The principal regulations governing this are the Competition Act 1998 (Concurrency) Regulations 2014,[15] which provide that any competent person (ie concurrent regulator) must inform any other such competent person before exercising powers to enforce the CA98 or TFEU prohibitions. Where more than one regulator may act, they should agree which one will so act, on the basis of which one is better placed.[16] No regulator may act until it has been agreed which regulator will do so, and once a case has been allocated to a regulator, no other regulator may act.[17] In case of dispute, ultimately the CMA must decide.[18] Allocation of investigations under the TFEU prohibitions is governed by Regulation 1/2003.[19]

In anticipation of its new powers earlier this year the FCA consulted on draft guidance on CA98 and on market studies and making market investigation references, and on draft rule changes to reinforce disclosure obligations on authorised firms in relation to competition law infringements. The FCA published its policy statement responding to feedback received during the consultation, and its finalised guidance and rules, on 15 July 2015.[20]

In practical terms, the FCA has assembled a Competition Division of some 80 staff, comprising both new recruits and FCA staff who are active across the competition mandate

15 SI 2014/536.
16 See para 3.22 of *Regulated Industries: Guidance on concurrent application of competition law to regulated industries (CMA10)* [2014] UKCLR 811, available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/288958/CMA10_Guidance_on_concurrent_application_of_competition_law_to_regulated_industries.pdf.
17 Competition Act 1998 (Concurrency) Regulations 2014 (SI 2014/536), reg 6.
18 Ibid, reg 5.
19 Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (2003) OJ L 1/1, available at http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32003R0001&from=EN.
20 http://www.fca.org.uk/news/ps15–18-fca-competition-concurrency-guidance-handbook-amendments.

(ie market studies, embedding competition and CA98 enforcement). On CA98 cases, staff will work closely with colleagues from the Enforcement and Market Oversight Division.

In addition, the FCA is recruiting panellists for a Competition Decisions Committee (CDC), which will be the body that will take final decisions in CA98 cases. In technical terms, these people will be the 'different relevant person' (who must in fact comprise at least two relevant persons!) within the meaning of r 3 of the CMA Rules.[21] This is how the FCA will ensure decisional separation between the FCA staff who will decide whether to take a case on, investigate it and decide whether there is sufficient evidence to propose to make an infringement decisions (ie to issue a statement of objections) and the individuals who will finally dispose of a case.

It is too early to say how many CA98 cases the FCA will investigate: this will largely be driven by the specific cases identified. However, the FCA hopes that its new powers and team should lead to increased detection, enforcement, and deterrence, within the financial services sector, for the benefit of consumers.

Practical challenges of concurrency

Competition concurrency presents questions and issues to be addressed both for the FCA and for firms and their advisers. The first cases and early years of any new regime are likely to be challenging. The FCA has a new team (albeit including experienced individuals). It also has significant enforcement experience, but there is no FCA corporate experience of CA98 enforcement. Accordingly, the FCA will be conducting CA98 enforcement processes for the first time.

Identifying cases

The FCA has the challenge common to all competition authorities of identifying potential cases. It should, however, be as well-placed as any other, if not more so. Firms can now complain to the FCA in the knowledge that it has the power to act under CA98 as well as under its regulatory powers. In addition, the FCA has ongoing relationships with the firms and persons it regulates, and its departments may identify issues as part of their other activities. Its market studies (see above) may unearth issues for investigation under CA98.

Finally, and possibly surprisingly for competition lawyers, a firm regulated by the FCA under FSMA has assumed a duty under Principle 11 of the Principles for Businesses to deal with its regulators in an open and co-operative way, and must disclose to the FCA appropriately anything relating to the firm of which the FCA would reasonably expect notice.[22] The FCA considers that this extends to facts or circumstances suggesting that they may have committed a significant infringement of competition law.

Similarities with and differences from FSMA enforcement

The FCA can draw on its experience of FSMA enforcement. At a high level, the processes are similar: they can involve extensive fact finding, detailed and complex analysis, and well-resourced and resourceful subjects of investigation. However, there are differences.

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21 Competition Act 1998 (Competition and Markets Authority's Rules) Order 2014 (SI 2014/458), available at www.legislation.gov.uk/uksi/2014/458/schedule/made.

22 Similarly, a person in relation to whom the FCA or the Prudential Regulation Authority (PRA) has given approval to perform a controlled function under FSMA has a duty under Principle 4 of the Statements of Principle for Approved Persons to deal with the FCA, the PRA and other regulators in an open and co-operative way, and must disclose appropriately any information of which the FCA or the PRA would reasonably expect notice. These are well-established Handbook rules which are intended to ensure that they are made aware of matters that might be relevant to their role as regulator.

In CA98 cases, parties have full access to the disclosable documents on the file that relate to the matters contained in the statement of objections, while they do not in FSMA cases.[23] Moreover, the degree and manner of separation of decision-making between a proposed and final decision differs. For FSMA cases, the FCA has its Regulatory Decisions Committee (RDC). This issues both warning notices and final decision notices, but unlike the planned CDC, it is kept at arm's length from the FCA staff team that conducted the initial investigation. In CA98 cases, the CDC will have access to the staff team that has investigated since the outset.

Appeal in CA98 cases is to the Competition Appeal Tribunal (CAT), and is a full merits review. For FSMA cases, RDC decisions can be referred to the Upper Tribunal (Tax and Chancery Chamber). The Upper Tribunal is an independent judicial body established by the Tribunals, Courts and Enforcement Act 2007, which hears references afresh, that is, de novo. Both the CAT and the Upper Tribunal can hear evidence from witnesses.

Leniency and Principle 11

A further difference is that in CA98 cases, leniency may be available for those who admit participation in cartels and fulfil the conditions specified by the CMA in its leniency policy.[24] The FCA does not offer leniency with regard to its other enforcement activities. Instead, it considers that the firms it regulates are duty-bound to report possible infringements under Principle 11 (although, unlike for a grant of a leniency marker,[25] there is no requirement to admit to any infringement). Equally, Principle 11 may have a role in assisting the FCA to detect and terminate anti-competitive conduct (as well as enhancing firms' incentives not to engage in such conduct in the first place).

The interaction between the CMA's leniency programme and the Principle 11 obligation has been the subject of some comment. A key distinction is that the former is voluntary while the latter is mandatory for those who have chosen to be active in the sector. Firms, for their own reason, might choose not to apply for leniency and hope to evade detection. Although regulated firms enjoy the same freedom as to whether or not to apply for leniency, they may be subject to penalties if they fail to comply with their Principle 11 obligations.

While we appreciate that firms may need to think carefully in navigating the two procedures, we think that with common sense, transparency with the relevant authorities, and good co-operation between the relevant authorities (ie the FCA and CMA), this should be practicable if they act promptly. For example, firms considering applying for leniency should have regard to the CMA's guidance,[26] so as to ensure that they do not prejudice their (or their employees'[27]) ability to obtain immunity or leniency. For its part, the FCA would collaborate with the CMA in the event of a notification of cartel activity, and would not require any firm to take actions that might tip off fellow cartelists without consulting the CMA. Nevertheless, this situation will only arise for those firms that have taken part in cartels: if a firm can avoid such activity, it will not find itself in any such awkward position.

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23 In FSMA cases, the FCA must disclose material on which the FCA relied in taking the decision to give a statutory notice and any material which in the FCA's opinion might undermine that decision.

24 *OFT's guidance as to the appropriate amount of a penalty* (OFT423) September 2012, [2013] UKCLR 1 and *Applications for leniency and no-action in cartel cases* (OFT1495), available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/284417/OFT1495.pdf.

25 In addition to a concrete basis for a suspicion of cartel activity, the grant of a leniency marker requires a genuine intention to confess (see OFT1495, para 3.11).

26 See OFT1495, and in particular paras 3.8–3.14 on conducting internal investigations and paras 3.24–3.28 on maintaining confidentiality and securing evidence.

27 We note that only the CMA can enforce, or grant leniency in respect of, the criminal cartel offence contained in EA02, s 188.

The CMA and the FCA share an interest in deterring, detecting, destabilising and ending cartels, and as such are keen to preserve the incentives for firms to apply for leniency. The FCA and CMA have therefore agreed restrictions on the use that may be made of leniency information shared for competition enforcement purposes.

Concurrent powers or FSMA powers; primacy

The FCA now has a very broad range of tools which it can use to investigate and, if necessary, remedy competition issues. It may enforce the competition prohibitions in CA98 and TFEU, and use its FSMA powers. It may conduct market studies under FSMA or EA02. It can make market investigation references to the CMA. Further, as supervisors of authorised firms, the FCA also has 'softer' tools available, so there is not always only a choice between (in advance) rule-making and enforcement under CA98 or FSMA (after the event).

The FCA's choice of tool appears fairly unconstrained by statute. There is a 'primacy' obligation in FSMA, s 234K, which states that before exercising any one of six specified FSMA powers,[28] the FCA must first consider whether acting under CA98 would be more appropriate. If the FCA considers that CA98 action would be more 'appropriate', then it must not exercise such FSMA power. 'Appropriate' is not defined for the purposes of s 234K. There is no equivalent primacy obligation with regard to the choice between conducting a FSMA or EA02 market study.

Given this broad choice, the key question is which tool most efficiently and effectively allows the FCA to investigate and if necessary remedy the possible harm that it has identified. Some issues might fall naturally under CA98 (eg collusive practices aimed at fixing pricing or allocating markets); others might only be addressed under FSMA (unilateral conduct by a non-dominant firm). The limited differences we have identified between EA02 and FSMA market studies might influence the FCA's choice (for instance, the formal powers under EA02 to gather information from firms beyond the FSMA perimeter).

We are aware of the widespread desire for more CA98 enforcement action, and support it.[29] Establishing CA98 precedents may have a deterrent effect on others within and beyond the relevant market, and assist firms and their advisers within the financial services sector and across the economy by clarifying and developing areas of competition law. It is very difficult to quantify such benefits, and to weigh them against efficiency benefits (in terms of the FCA's and firms' resources) that may come from using other tools available to stop the same harm to consumers. Accordingly, we expect that the FCA will consider carefully what is the most appropriate intervention for the issue in question, and that identifying the appropriate tool for any particular situation will be very fact-specific and involve considering the harm in question, potential outcomes and deterrent effect.

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28 The six powers are: FSMA, s 55J(2) to vary or cancel a Part 4A permission (to carry out regulated activities); s 55L to impose or vary a requirement on an authorised person with a Part 4A permission; s 88E to take action against a sponsor firm (to advance the FCA's operational objectives); s 89U to take action against a primary information provider to advance the FCA's operational objectives; s 192C to give a direction to a qualifying parent undertaking; and s 196 to impose a requirement (intervention in respect of incoming firms).

29 See for example the National Audit Office's *Review of the UK's Competition Landscape*, March 2010, available at www.nao.org.uk/wp-content/uploads/2010/03/0910_competition_landscape.pdf, which found that concurrent regulators had 'used their competition enforcement powers sparingly, with the risk that case law is not as rich as it needs to be . . . for an effective competition system'.

Working with the UK Competition Network and European Competition Network

In assuming concurrent powers, the FCA joins the 'family' of concurrent UK regulators, and has also become a member of the European Competition Network (ECN). This means that it has access to the broader experience and expertise of such regulators, and can receive and share information with them.[30]

As noted, enforcement cases may be allocated to different authorities (and even subsequently transferred between authorities). Accordingly, the FCA will consider whether it is possible or appropriate for others, such as the CMA, to act on any issues it identifies. It expects to co-operate closely with the CMA and other concurrent regulators if appropriate, to avoid duplication and unnecessary burdens on firms, or issues being missed.

The FCA already co-operates closely with the CMA, both on general concurrency issues (via the UK Competition Network (UKCN)), but also on specific investigations. One example is the joint market study in SME (small and medium-sized enterprise) banking (during which the FCA and CMA collaborated closely to ensure that they made best use of their respective resources and avoided duplication, for instance with regard to information requests). This was followed by the market investigation reference to the CMA for in-depth investigation of retail banking.[31] The FCA continues to assist, providing a technical workshop for the CMA's market investigation panel members in order to share its market knowledge and expertise of the applicable regulation. Equally, the FCA has provided knowledge and output from relevant work, such as its review of the Current Account Switch Service and account number portability.

Future competition work

In its business plan, the FCA announced a full programme of competition work for 2015/16.[32] It will continue its credit card market study, and implementing remedies following its final reports in the cash savings and retirement income market studies. Following on from its wholesale sector competition review, it has launched a market study into investment and corporate banking services and plans to launch a study into asset management services. It will undertake a market study to investigate how insurance firms use Big Data, such as web analytics and behavioural data tools (including the increasing use of social media) as well as other unconventional data sources.

With regard to retail lending, the FCA will continue to assess how firms are implementing its post-Mortgage Market Review rules.[33] From autumn 2015 it will begin a wider assessment of barriers to competition (such as factors affecting consumers' ability to access credit and ability to switch providers, and barriers to entry and/or expansion) with a view to launching a market study in early 2016 on those aspects of the mortgage market that are not working to the benefit of consumers.

With regard to enforcement cases under CA98 and TFEU, this will depend on complaints received and own initiative work. While the FCA is working on a pipeline of cases, it cannot predict the number and type of formal investigations that might result.

30 Information law is a sophisticated discipline in its own right. For present purposes, we note only that the FCA takes it very seriously, and that any information it discloses or uses will be handled in accordance with the provisions of Part 23 of FSMA, and/or Part 9 of EA02. This extends to sharing information with other authorities, although there may be specific gateways available. In addition, the provisions of FSMA, s 118 may apply (which regulate insider trading), as well as those of the Data Protection Act 1998.

31 See www.gov.uk/cma-cases/review-of-banking-for-small-and-medium-sized-businesses-smes-in-the-uk.

32 See www.fca.org.uk/static/channel-page/business-plan/business-plan-2015–16.html.

33 See www.fca.org.uk/firms/firm-types/mortgage-brokers-and-home-finance-lenders/mortgage-market-review.

Conclusion

It will take some time before the FCA's competition work is recognised to be at full strength. Some of its powers are new and it is using others in new ways, to promote competition. There are many different financial services markets with varied characteristics, and the FCA has to choose where best to devote its resources. That said, during the first two years of the FCA it has come a long way in building a competition capability and deploying it across the various fronts outlined in this article. The FCA has the powers it needs to make a real difference to competition in the financial services sector, for the ultimate benefit of consumers.