Antitrust Policy and ESG Cooperation in the Financial Sector

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"La calomnie, monsieur ! Vous ne savez guère ce que vous dédaignez ; j'ai vu les plus honnêtes gens près d'en être accablés" Beaumarchais, *le Barbier de Séville*

In November 2021, at the COP in Glasgow, Mark Carney, special UN Envoy for Climate Action and Finance and ex-Governor of the Bank of England (and who was amongst the first to warn about the impact on climate change on financial actors), announced the creation of the Glasgow Financial Alliance for Net Zero (GFANZ). This Alliance regroups more than 500 large financial actors worldwide (banks, insurers, asset owners, asset managers, financial services providers and investment consultants), representing around 40% of global financial assets and committed to work together to support the transition decided in the Paris climate agreement to a climate change limited to 1,5° and to a net zero economy in 2050. The Alliance was founded to expand the number of net zero-committed financial institutions and to establish a forum for addressing sector-wide challenges associated with the net zero transition. GFANZ has worked to develop the tools and the methodologies needed to turn financial institutions' commitments into action.

The GFANZ and other alliances between financial actors have been confronted in the United States by recent antitrust initiatives by Republican Senators and House Representatives and by State Attorneys General (1), who have shown the will of using antitrust laws to oppose ESG (Environment, Social, Governance) efforts of cooperation between important financial actors. In October 2022, 19 State AGs served subpoenas on six US large banks seeking information in the Net-Zero Banking Alliance, which is a sub-group of the GFANZ. In March 2023, a letter from 21 states Attorneys General to various asset-managers confirmed their will of using antitrust law to oppose ESG efforts.

There is an evident political background of this initiative: these States are governed by Republicans, who are climate-skeptical and opposed to ESG initiatives by all possible means.

But the threat of antitrust litigation cannot be taken lightly. The typical advice of a lawyer to a firm on this kind of issue would be to be cautious.

The threat of antitrust litigation seems to have had an impact on the GFANZ. A significant number of members have left the Alliance in the last months due to this threat and/or other reasons.

The European Commission and the United Kingdom Competition and Market Authority have recently taken position on this issue. The UKCMA has published a draft guidance in February 2023. The European Commission has revised its Horizontal guidelines in June, after consultation, to give a specific guidance on sustainable agreements. Guidelines are not laws and they do not as such put in place any obligation on the companies. But they put obligations on the authorities which have issued them insofar as they are obliged to interpret the law as they have announced that they would, and so they are useful tools for companies.

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The content of the antitrust challenges in the United States

The AGs March letter expresses concern that participation of asset-managers in ESG initiatives could constitute collusive behavior in violation of antitrust laws, as they exert "coordinated pressure" on companies to reduce greenhouse gas emissions and "commit to forcing" these companies to align with their ideals. One of these initiatives, Climate Action 100+, is described as "an agreement to limit… the asset stewardship services offered by asset-managers" and that this will have adverse effects on competition.

The letter also suggests that **companies may be orchestrating "group boycotts"**, when refusing to deal with entities which do not support ESG initiatives.

The letter warns in addition asset-managers that unilaterally using proxy advisor guidance that aligns to Climate Action 100+ or Net Zero Asset Managers (NZAM) commitments in voting may be deemed a violation of antitrust laws.

Finally, the State AGs argue that **"there appears to be less restrictive means" to accomplish most of the goals related to disclosure.**

Some Republican AGs, Senators or House Representatives have put forward more stringent arguments, alleging for instance that Climate Action 100+ "pressured companies to shut down coal and natural gas plants... and that these activities likely were contributing to rising gas prices" (Arizona AG in May 2022).

It must be recalled that **State Attorney Generals do not decide any case**. This is for the courts in their judgements. There is a long way to go before a judgement issued by a court. But of course, companies can want to avoid a litigation on such an issue.

Up to now, **the antitrust authorities of the United States have not published any position** on this matter.

1. The flexible approach of the United Kingdom Competition and Markets Authority

In February 2023, the UK Competition and Markets Authority (CMA) has published for consultation draft guidance on environmental sustainability agreements (2).

Modeled on the competition rules of the Treaty of the European Union, the Competition Act 1988 prohibits certain agreements that have "as their object or effect the prevention, restriction or distortion of competition". But these agreements can be exempted if "they contribute to improving the production or distribution... or to promoting technical progress, while allowing consumers a fair share of the resulting benefit", provided that they do not impose any restrictions on that are not indispensable to achieve those objectives and do not eliminate competition.

In the most important part of the draft guidance, the CMA explains its approach to the four criteria that must be established for the exemption to apply:

- the agreement must give rise to benefits to production, distribution or technical or economic progress;
- the restriction of competition arising from the agreement must be indispensable to achieve these benefits;
- consumers must receive a fair share of the benefits;
- there must be no elimination of competition.

The analysis of these four conditions for ESG initiatives, and in particular for climate change agreements, by the CMA leads to the following conclusions:

- **CMA will consider environmental benefits to be efficiencies** (in line with existing jurisprudence);
- CMA give two interesting **examples of the indispensability of the agreements:** competitors entering into a collective purchasing agreement in order to increase demand and drive economies of scale for a more sustainable input (*e.g.*, a plastic replacement); an agreement between competitors to switch to a more sustainable, but more expensive input, where no single company would be incentivized to make this change alone, because there is a "first mover disadvantage";
- **CMA plans to exempt environment sustainability agreements if the "fair share to consumers" condition can be justified;**
- **The condition of the non-elimination of competition must always be fulfilled.**

The draft guidance asks the businesses to quantify the benefits of the agreement and demonstrate that they are sufficiently significant to offset the harm arising from the restriction of competition.

The approach of the CMA is more open to climate change agreements, because climate change "represents a special category of threat that sets it apart and requires a different approach".

First, the CMA plans to take into account the totality of the benefits to all UK consumers, not just those that are affected by the restriction of competition. To benefit from this approach, the partie to the agreement would need to demonstrate that the benefits are in line with legally-binding requirements or with well-established national or international targets.

Secondly, for the quantification of the benefits expected from climate change agreements, the draft guidance notes that in many cases it will not be necessary to do a precise quantification, for example when the agreement will give rise to a limited restriction of competition but a significant sustainability benefit.

The draft guidance provides also that the CMA intends to operate an open-door policy and invites businesses to make contact at an early stage in the development of environmental sustainability initiative, having first conducted an initial self-assessment of their agreement following the principles set out in the guidance, including a quantification of the expected environmental benefits.

Finally the CMA intends to publish anonymized summaries of sustainability agreements which have been shared with it for consultation, in order to develop a body of positive decisional practice.

In conclusion, the draft guidance intends to facilitate businesses' intention to address environment sustainability agreements and even more for climate change agreements. It is a clear rebuff of the position taken by Republican officials in the United States.

2. The position of the European Commission

In a speech in April 2023 (3), Margrethe Vestager, Vice-President of the European Commission and Competition Commissioner, said "antitrust rules should support the green transition". For her, "cooperation can be a good thing", notably to overcome "the first mover disadvantage" (same argument as the UKCMA). But she warns that "the last thing Europe needs is cartels using sustainability as a cover for illegal collusion".

She announced a reform of the Horizontal guidelines, which will include a new chapter on sustainability agreements. "We want to provide companies with a clear framework to assess their initiatives and we stand ready to engage with those companies that want to discuss and obtain guidance" (like the UKCMA).

In June, the European Commission adopted new Horizontal guidelines (4), which included a specific part on sustainability agreements. These guidelines are very detailed and give many practical examples, but none of them in the financial sector.

The most important points of these guidelines are the following:

1. The Commission recalls that **sustainable development is a core principle of the EU Treaty and policy and estimates that "sustainability agreements" can play a positive role in this regard.**

   Competition enforcement contributes to sustainable development by ensuring effective competition, which stimulates innovation and contributes to the consumer welfare. However, the Commission recognises that individual production and consumption decisions can have negative effects on factors like the environment. One way of addressing or mitigating such market failures is through collective action, including "sustainability agreements".

2. The Commission uses the term **'sustainability agreement' in the Guidelines to refer to any type of agreement between competitors that *genuinely pursues* one or more sustainability objectives.** And it says that the notion of a sustainability objective includes, but is not limited to addressing climate change, eliminating pollution, limiting the use of natural resources, respecting human rights, fostering resilient infrastructure and innovation, reducing food waste, facilitating a shift to healthy and nutritious food, and ensuring animal welfare.

3. **The Guidelines make clear that some types of sustainability agreements are generally permissible** (under Article 101(1)), including some examples which may seem obvious:

- agreements on internal corporate conduct that do not concern the economic activity of competitors, for example measures to eliminate single-use plastics in the business premises, to not exceed certain temperatures in the buildings, or to limit the number of printed materials;
- agreements to create databases containing information about suppliers with sustainable value chains, production processes, or inputs, without the requirement to purchase from those suppliers or sell to distributors; and
- organising industry-wide awareness campaigns on the environmental footprint of consumption, without joint advertising of particular products.

4. **More importantly, the Guidelines provide specific guidance on standardisation agreements in the sustainability field,** which are agreements where competitors agree to adopt and comply with certain sustainability standards, such as manufacturing methods or input standards intended to phase out, withdraw or replace non-sustainable products and manufacturing methods.

   The Commission's draft guidance clarifies that such arrangements are generally unproblematic from an EU competition law perspective provided the following cumulative conditions are met:

- the procedure for developing the sustainability standard is transparent and all interested competitors can participate in the process leading to the selection of the standard;
- there is no obligation on companies not participating in the standard to comply with the standard;
- participants remain free to adopt for themselves a higher sustainability standard than the one agreed among the participants;

- participants do not exchange commercially sensitive information that is not needed for the development, adoption or modification of the standard;
- access to the outcome of the standardisation procedure is effective and non-discriminatory;
- the standard does not lead to significant price increase or reduction in choice of products; and
- there is a mechanism monitoring the compliance with the standard by undertakings that have adopted it.

Failure to meet one or more of these conditions does not automatically mean that the arrangement is anticompetitive. However, if any of the conditions are not met, the sustainability standardisation agreement requires further justification to determine whether it could have a negative effect on competition.

5. **Even if an agreement has negative effects on competition, the Guidelines recognise that the sustainability aim can benefit consumers in several ways, and may therefore be exempted from the rules on anticompetitive agreements, if the parties prove that the traditional four cumulative conditions under Article 101(3) are satisfied:**

- the agreement in question contributes to improving the production or distribution of goods or to promoting technical or economic progress, such as use of cleaner production or distribution technologies, more resilient supply chains or better quality products;
- the agreement must not impose restrictions that are not indispensable to the attainment of the sustainability benefits under the agreement;
- consumers must receive a 'fair share' of the benefits under the agreement, which occurs when the benefits deriving from the agreement outweigh the harm, so the overall effect on consumers is at least neutral; and
- the agreement must not allow the parties to eliminate competition.

With regard to the consumer benefits, the most obvious are use-related benefits, such as the use of a healthier product. The less obvious (but still recognised) ones are non-use related benefits, such as a product that results in less water contamination or more limited deforestation.

The Guidelines also acknowledge that, in certain circumstances, **collective benefits of sustainability objectives can occur, irrespective of consumers' individual appreciation of the product**. The Commission gives the example of drivers purchasing less polluting fuel also benefitting from cleaner air, if less polluting fuel is used. To the extent that there is a substantial overlap of consumers (the drivers) and the beneficiaries (citizens), the sustainability benefits of cleaner air are in principle relevant for the competition assessment and can be taken into account if they are significant enough to compensate consumers in the relevant market for the harm.

Therefore, **the Commission essentially requires full compensation of the consumers on the relevant markets**, contrarily of the UK authority for climate agreements and despite some criticism during the consultation. Their position is that "full compensation" is a matter of judgement and is actually the nature of the balancing act between restrictions in Art.101(1) and benefits in 101(3) to compare negative quantifiable impact on prices with usually longer term more qualitative benefits for consumers.

6. The Guidelines also remind **companies wishing to enter into a sustainability agreement that they can request informal guidance** from the Commission in order to ensure compliance with EU competition rules. The provision of such guidance may complement the general framework of analysis set out in the new sustainability chapter. Commissioner Vestager explicitly envisaged adopting the first time positive decisions under Art.10 of Regulation 1/2003 if confronted with cases where the balance between restrictions and compensation described above is not crystal clear.

   This possibility offered by the Commission is of course to be welcome.

Conclusion

The antitrust controversy led by Republican officials in the United States has for objective to create an environment more difficult for the climate and the ESG alliances of financial actors.

In a recent article (5), Nathan Fabian (PRI, Principles for Responsible Investment) argues that these antitrust arguments are misguided and should not diminish the transition. He underlines that "one of the most effective ways to enable markets – and therefore long-term returns for investors – is for investors to come together to develop frameworks and encourage progress to the interest of their clients and beneficiaries... Collaboration creates the potential for more simplicity and efficiency for companies".

The new horizontal guidelines of the European Commission, as also the draft guidance of the Competition Market Authority of the United Kingdom, go in the same direction and have clarified their position which in general contradict the position of the US Republican officials. They notably underline the benefits that can be produced by sustainable agreements between competitors, they define some "safe harbour" cases and at least they give rather clear check-lists that firms, including financial entities, must carry out before entering in sustainability agreements.

They also offer to the firms the possibility to request informal guidance from them before entering into sustainability agreements.

These new guidelines should comfort ESG cooperation in the financial sector.

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