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The SEC and DOJ Sign Historic Memorandum of Understanding to Enhance Competition in Securities Markets: BakerHostetler

On June 22, 2020, the Securities and Exchange Commission (“SEC”) and Antitrust Division of the Department of Justice (“DOJ”) Antitrust Division announced that they have signed an interagency Memorandum of Understanding (“MOU”) to “foster competition and communication between the agencies” in an effort to enhance competition in the securities industry.[1] This is the first MOU between the DOJ’s Antitrust Division and the SEC.

While the two enforcement agencies have worked together in the past, Assistant Attorney General Makan Delrahim stated that the MOU “institutionalizes a strong working relationship between” the agencies, which he expects will result in “robust, comprehensive analyses” regarding competition and securities law concerns.[2] According to Delrahim, this in turn could result in “healthier markets yielding enhanced consumer benefits.”[3] SEC Chairman Jay Clayton also noted the MOU’s goal of “greater collaboration and cooperation” between the agencies and the desire to ensure efficiency and competitiveness in U.S. markets.[4]

Competition in the Securities Markets

The presence of competition in the securities markets benefits customers on many levels, including competition on price, quality, service, and innovation.[5] Delrahim noted that firms that fear losing their market position are more likely to engage in these activities, thereby benefitting customers.[6] For example, firms may invest more in research and development to introduce new products or services to meet customer needs, seek out ways to streamline production processes, enhance the quality of their offerings, and pursue ways to make their products and services desirable.[7]

The SEC has consequently listened to concerns from market participants on where competition may be absent or diminished and has engaged in reviews of these concerns and the underlying industries to determine whether competition is lacking. This has led to various rule-making actions by the SEC, including the Market Data Proposal,[8] which is designed to update the national market system (“NMS”) for the “collection, consolidation, and dissemination of information with respect to quotations for and transactions in [NMS] stocks.”[9] The proposal also seeks to introduce competitive forces NMS for the first time. According to the SEC, the introduction of competition could allow all market participants — including investors — to access and benefit from the expanded content of NMS market data.[10] The Antitrust Division lauded the Market Data Proposal in its public comments, noting that it seeks to lower barriers to market entry, which improves quality of and access to inputs, such as information — a classic way to enhance competition.[11] This is a signal that the SEC is seeking to revisit and revise older regulations in an effort to enhance competition in the U.S. markets.

The Antitrust Division also commented on the procompetitive effects of the SEC’s Proxy Rules Proposal,[12] which, according to the SEC, is designed to “help ensure that proxy voting advice used by investors and others who vote on investors’ behalf is accurate, transparent, and materially complete.”[13] Delrahim noted that the proposed rule is also designed to update regulations to

better fit the current landscape and lead to healthier competition.[14] In other words, while certain of the details of the markets have changed, competition remains wholly relevant.[15]

Increased Coordination Could Lead to Increased Investigations

Adopting the approach of continuously reviewing rules and regulations for their applicability and relevance in today's markets, the SEC and the Antitrust Division entered into the MOU — the first of its kind — to establish regular communication between the agencies to allow for information sharing. Specifically, the MOU is targeted at facilitating communication and cooperation between the agencies, by establishing a framework for the SEC and the Antitrust Division to continue discussions and review regulatory matters that affect competition in the securities industry.[16] This includes provisions to establish periodic meetings among the agencies' officials.[17] Additionally, the MOU provides for the exchange of information and expertise the agencies may believe relevant to their oversight and enforcement responsibilities, as consistent with legal and confidentiality restrictions.

Delrahim noted that the Division has taken on several complex criminal investigations in the financial services industry, including recent investigations into foreign currency exchange, interest rate benchmarks, and municipal bonds. For example, the agencies worked closely on an investigation of anticompetitive activity in the municipal bond investments market, which resulted in the conviction of one financial services firm and 17 individuals, and in restitution, penalties, and disgorgement related to four other financial institutions under non-prosecution agreements.[18] With help from the SEC, among others, the financial services firm agreed to pay restitution to victims of the anticompetitive conduct and to cooperate with the Antitrust Division regarding ongoing investigations into anticompetitive conduct in the municipal bonds industry. This could mean that the MOU serves as further justification for referrals between agencies that may result in criminal prosecution.

Is noteworthy that shortly after Delrahim's remarks, The Wall Street Journal suggested that the MOU may lead to antitrust scrutiny of fees charged by exchanges for information, including market data.[19] Chairman Clayton has previously noted that the SEC has an obligation under the Securities Exchange Act of 1934 "to suspend exchanges' fee filings unless it is established that the fee is reasonable on another basis, such as a reasonable cost basis,"[20] although, Section 11A of the 34 Act never uses the term "cost basis." Rather the law states that market data must be disseminated by securities information processors and securities exchanges on "fair and reasonable terms" and make that data available on terms that are not "unreasonably discriminatory." The government takes the position that the burden is on the exchange to demonstrate competitive forces or an alternative basis for finding the fee reasonable, while exchanges may well disagree. Exchanges argue that markets functioned well through the highest periods of volatility during the pandemic crisis and continue to do so. Further, they argue that significant changes to well-functioning market infrastructure, particularly during a pandemic, could introduce untold operational and technical risks, confusion and the likelihood for an unfriendly investor experience. Market structure reform raises highly complex, competitive and regulatory issues. This MOU could potentially result in litigation by and against the SEC or enforcement actions. In recent testimony before the Subcommittee on Investor Protection, Entrepreneurship and Capital Markets, SEC Chairman Clayton noted that the signing of the MOU with the Justice Department does not "imply that we are investigating anybody together." [21] When asked about potential anticompetitive behavior that may have been contemplated, Chairman Clayton informed the Subcommittee that they do not comment on investigations but rather the MOU "formalizes that powerful relationship that we have across our respective agencies." [22]

Conclusion

Although specific detail has not yet been provided on how the MOU will be put into effect, a number of circumstances now seem more likely:

- **Rule Changes:** The Antitrust Division and the SEC will likely continue to evaluate rules and regulations they deem outdated due to technological advances in the marketplace. There are, however, challenges in achieving this goal. Specifically, markets and data move quickly, which means that the agencies will need to move quickly to monitor industry developments and their effects, particularly in an effort to understand when intervention is appropriate and required.[23]
- **Parallel Investigations:** The agencies will share information on a more frequent basis, which may in turn lead to a greater number of investigations that could very well be done in parallel by both agencies. However, given confidentiality considerations as laid out in the MOU, it will be interesting to see how, if at all, the cooperation contemplated in the MOU will successfully interact with the Antitrust Division's Leniency Program and/or the SEC's whistleblower and cooperation program.

[1] U.S. Sec. & Exch. Comm'n., Press Release, Rel. No. 2020-140, "Securities and Exchange Commission and Justice Department's Antitrust Division Sign Historic Memorandum of Understanding" (June 22, 2020), available at <https://www.sec.gov/news/press-release/2020-140>; U.S. Dep't. of Justice, Justice News, "Justice Department's Antitrust Division And The Securities And Exchange Commission Sign Historic Memorandum of Understanding" (June 22, 2020), available at <https://www.justice.gov/opa/pr/justice-department-s-antitrust-division-and-securities-and-exchange-commission-sign-historic>. The MOU is available at <https://www.sec.gov/files/ATR-SEC%20MOU-06-22-2020.pdf>.

[2] Id.

[3] Id.

[4] Id.

[5] U.S. Dep't. of Justice, Justice News, "Changes in Latitudes, Changes in Attitudes: Enforcement Cooperation in Financial Markets (June 22, 2020), available at <https://www.justice.gov/opa/speech/changes-latitudes-changes-attitudes-enforcement-cooperation-financial-markets> ("Delrahim Speech").

[6] Id.

[7] Id.

[8] 17 CFR Parts 240, 242, and 249; Rel. No. 34-88216.

[9] Id. at p. 1.

[10] U.S. Sec. & Exch. Comm'n., Press Release, Rel. No. 2020-34, "SEC Proposes to Modernize Key Market Infrastructure Responsible for Collecting, Consolidating, and Disseminating Securities Market Data" (Feb. 14, 2020), available at <https://www.sec.gov/news/press-release/2020-34>.

[11] Supra note 5.

[12] 17 CFR Part 240, Rel. No. 34-87457.

[13] U.S. Sec. & Exch. Comm'n., Press Release, Rel. No. 2019-231, "SEC Proposes Rule Amendments to Improve Accuracy and Transparency of Proxy Voting Advice" (Nov. 5, 2019), available at <https://www.sec.gov/news/press-release/2019-231>.

[14] Delrahim Speech.

[15] Id.

[16] Id.

[17] Id.

[18] Delrahim Speech; see also U.S. Dep't. of Justice, Justice News, "GE Funding Capital Market Services Inc. Admits to Anticompetitive Conduct by Former Traders in the Municipal Bond Investments Market and Agrees to Pay \$70 Million to Federal and State Agencies" (Dec. 23, 2011), available at <https://www.justice.gov/opa/pr/ge-funding-capital-market-services-inc-admits-anticompetitive-conduct-former-traders>.

[19] Dave Michaels and Alexander Osipovich, The Wall Street Journal, “SEC, Justice Department to Scrutinize Exchanges’ Market-Data Business” (June 22, 2020), available at <https://www.wsj.com/articles/sec-justice-department-to-scrutinize-exchanges-market-data-business-11592864481>.

[20] U.S. Sec. & Exch. Comm’n., Speech, “Modernizing U.S. Equity Market Structure” (June 22, 2020), available at <https://www.sec.gov/news/speech/clayton-redfearn-modernizing-us-equity-market-structure-2020-06-22>.

[21] See “Hybrid Hearing - Capital Markets and Emergency Lending in the COVID-19 Era,” June 25, 2020, before the Subcommittee on Investor Protection, Entrepreneurship and Capital Markets, Committee on Financial Services, U.S. House of Representatives, available at: <http://archives-financialservices.house.gov/media/pdf/072601rb.pdf>.

[22] Id.

[23] Delrahim Speech.

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