

**Unclassified****English - Or. English**

26 September 2018

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS  
COMPETITION COMMITTEE****Summary of Discussion of the Hearing on Common ownership by institutional  
Investors and its Impact on Competition****Annex to the Summary Record of the 128th Meeting of the Competition Committee held on  
5-6 December 2017**

This document prepared by the OECD Secretariat is a detailed summary of the discussion held during the 128th meeting of the Competition Committee on 6 December 2017.

More information related to this discussion can be found at [www.oecd.org/daf/competition/common-ownership-and-its-impact-on-competition.htm](http://www.oecd.org/daf/competition/common-ownership-and-its-impact-on-competition.htm)

Please contact Mr. Antonio Capobianco [[Antonio.Capobianco@oecd.org](mailto:Antonio.Capobianco@oecd.org)] if you have any questions regarding this document.

**JT03436176**

## *Summary of Discussion of the Hearing on Common ownership by institutional Investors and its Impact on Competition*

*By the Secretariat*

The **Chair** of the Competition Committee, Professor Frédéric Jenny, opened the discussion by noting that common ownership – i.e. the ownership by institutional investors of minority shares in multiple competing firms – is a rapidly evolving topic of debate in the antitrust literature. He noted that common ownership is a distinct topic from cross-ownership, which was discussed by the Committee in 2008. He welcomed the panel of experts who represent various viewpoints on the topic, including the views of institutional investors. He also thanked the delegations which submitted country contributions.

The Chair explained that the Hearing would be organised in three parts; 1) theories of harm and empirical analyses of the impact of common ownership, including the critiques of the arguments, 2) views of the delegations and industry representatives, and finally 3) potential policy solutions as well as the drawbacks of the proposals. He emphasised that the discussion would primarily serve to introduce the various arguments in the literature, allowing delegates to take their own conclusions from the debate.

The Chair then invited the Secretariat to introduce the topic. The **Secretariat** summarised the key findings of the background paper, emphasising that the possible competition concerns raised by common ownership might be the most pronounced in concentrated industries.

The Chair thanked the Secretariat for setting the stage for the discussion and noted that common ownership is also being considered by various other OECD committees, including the Committee on Corporate Governance, which may look at common ownership from a different perspective. In case of cross-cutting issues such as this, the Chair noted that it is important to consider different point of views to find a common ground on how to move forward.

Before giving the floor to the panellists, the Chair asked them to disclose any industry affiliation they might have. Daniel O'Brien noted that two of his articles on common ownership were funded in part by the Investment Company Institute (ICI), though they are being prepared for submission to a peer-reviewed journal and are no longer funded by ICI.

### **1. Theories of harm and empirical analyses of the impact of common ownership and the related critiques**

To begin the discussion, the Chair invited **Professor Martin Schmalz** from the University of Michigan to summarise the main findings of the empirical research on the potential harms of common ownership. Professor Schmalz started highlighting some key facts and what are, in his view, misconceptions about the topic. First, he noted that competition requires incentives to compete. While separate owners can give firms such incentives, Professor Schmalz opined that common owners may not.

With regards to arguments that “the ownership of shares doesn’t correlate with control”, Professor Schmalz showed examples in which the largest 10 shareholders of competitors hold enough stock to jointly control a firm.. He underlined that anti-competitive effects can also arise as an “error of omission” by not pushing firms to compete, without explicit intent on behalf of investors and without collusion among firms. In other words, common owners may, not encourage firms to compete, since they have no incentives to become involved in a firm’s competitive strategy. There is no evidence that common owners push for more aggressive competition, but there is evidence to the contrary. He cited an example from the airline industry in which a decision that caused a stock decline in one airline would have been compensated with increases in the shares of its competitors, from the point of view of an investor that owned stock in all firms in the sector.

He also noted that these are not new theories. He referred to studies dating back 30 years which found that common ownership causes monopoly outcomes, and that mutual funds that concentrate on specific industries do the most harm. He emphasised that it is not necessarily an airline industry-specific issue; in the US, for example, banking markets show very similar ownership structures and price effects.

The Chair then asked **Professor Einer Elhauge**, from Harvard Law School, to provide his perspective on the potential competition impacts of common ownership. Professor Elhauge began by clarifying the difference between horizontal shareholding and common shareholding. While common shareholding can be between firms that are vertically related or related to a conglomerate, horizontal shareholding refers to situations when the leading shareholders of horizontal competitors overlap.

Professor Elhauge focussed part of his remarks on executive compensation, specifically incentive-based compensation, and explained that this may encourage managers to take into account not just the performance of their firms, but also that of the industry. In his view, this could be connected to horizontal shareholding, since horizontal shareholders actually profit more if the industry does well, compared to cases in which just an individual firm does well. He noted that these compensation mechanisms provide direct incentives to lessen competition.

In terms of the level of horizontal shareholding, he explained that over the period from 1999 to 2014, there was a dramatic rise – from 16% to 90% – in the likelihood that two large competing firms have a large horizontal shareholder. Over the same period, the gap between corporate investment and corporate profits has increased. Furthermore, regression analysis has established that the gap between corporate investment and profits is driven by the level of horizontal shareholding in concentrated industries.

The Chair then turned to **the United Kingdom** to describe the degree of common ownership in the UK economy. The Competition and Markets Authority (CMA) examined the ownership structure of three key UK industries; banking, insurance and grocery retailing. With respect to the banking market, they found that there is evidence of common ownership, but the sector is less concentrated than in the United States. Further, most of the common owners have investments in only a couple of banks. Compared to the banking market, the extent of common ownership on the general insurance and grocery retail sectors is less apparent.

According to the CMA, common ownership raises the following questions; (1) can ‘maverick’ firms with concentrated owners be enough to alleviate any competition concerns, (2) what is the transmission mechanism through which investors with relatively

small shareholdings influence firms' management, (3) what is the role of proxy voting, and (4) how important is within-industry diversification for prudential soundness.

Then **Germany** was asked to present the 2016 study of the German Monopolies Commission (Monopolkommission) on common ownership. The report concluded that, despite having small shares and limited formal ability to influence strategic decisions, the common ownership of shares by institutional investors may have the potential to distort competition. If investors hold shares in several companies operating in the same market, they will have an interest in maximising the returns of all shares. Thus, the investor will consider competition between the portfolio companies undesirable, because prices and profit margins of portfolio companies would fall, and if several indexes hold shares in several companies operating in the same market, the risk of eliminating competition is even higher because investors could have a common interest in reducing competition in the sector as a whole.

The Monopolies Commission carried out an empirical analysis to assess whether there were problematic "constellations" of horizontal minority shares held by institutional investors in Germany. The data showed that common ownership is particularly pronounced in the manufacturing industry, especially in the manufacturing of data-processing, optical, and electronic equipment, as well as machinery and vehicles. While this level of common ownership does not necessarily point to competition problems in these sectors, it does suggest that there is a need for further research and clarification before making any concrete recommendation for action.

Next, **Daniel O'Brien**, Executive Vice President at Compass Lexecon, took the floor to share his views on the theoretical and the empirical arguments regarding the competitive effects of common ownership. Dr. O'Brien began by noting that it is not a subject of disagreement that common ownership in concentrated markets can harm competition, if the ownership levels are high enough. The controversy centres on the competitive effects of common ownership that involves *minority shareholdings*. He emphasised that much of common ownership occurs through institutional investors that yield large benefits for retail investors. Institutional investors have brought portfolio diversification to the masses. An institutional investor can take positions in a basket of stock and diversify portfolios of thousands of retail investors all at once, which generates significant benefits.

According to Dr. O'Brien, a critical and yet unsettled question in this debate is how firms behave when owners have divergent interests. Specifically, 1) to what extent do common owners exert the control that is required to generate anti-competitive effects, and 2) to what extent does the firm place weight on non-common owners that may have different interests relative to common owners. It is critical to understand how minority ownership translates into control, since there is no basis for assuming that ownership is proportionate to control.

Dr. O'Brien also provided some additional reasons for scepticism over claims that common ownership has anti-competitive effects. First, he highlighted that laws on fiduciary duty require firms to behave in the interests of the firm and of the shareholders of the firm. Paying attention to what common owners want at the expense of non-common owners would technically violate this fiduciary duty. Dr. O'Brien also raised the question of whether or not minority ownership would translate into the kind of influence that would be required to have anti-competitive effects. Even if it translates into control, Dr. O'Brien opined that the question is about the incentives of institutional investors and whether or not contacts emerge that provide managers with incentives to take actions that are anti-competitive. He noted that there is a large variety of funds and institutions, some of which involve common ownership, cross-ownership, ownership of multiple firms, and others that

do not. Thus, it would be difficult for management to choose which shareholder would benefit in the case of potential anticompetitive conduct. This is particularly so because investors may not only hold shares in horizontal competitors, but also in suppliers and in customers. Finally, Dr. O'Brien called into question the empirical models showing harm from common ownership, and specifically their treatment of the modified Herfindahl-Hirschmann index.

Also on the side of scepticism, **Professor Daniel Rubinfeld** from New York University presented some of the views he has developed with his co-author Edward B. Rock (also from NYU). He clarified at the outset that he would focus his remarks on the airline industry, with which he has considerable expertise, including many antitrust cases as an enforcer.

Professor Rubinfeld discussed whether the ownership of minority shares by institutional investors in an oligopolistic market with four large carriers would have an effect on airline pricing. The structure of the US industry; i.e. three large legacy carriers, several low cost carriers (LCCs) and numerous ultra-LCCs, makes it hard to sort out empirically. A lot of empirical studies have found that the profitability of a certain route depends heavily not only on the number of competitors, but also on the presence or lack of presence of LCCs as well. Even the threat of entry of LCCs makes a difference, which alone has been able to depress prices on routes.

Professor Rubinfeld indicated that there is no compelling evidence of a relationship between market power and common ownership. In his view, the key issue, i.e. the causal relationship between common ownership and market power, is still unresolved. He pointed out that there are some routes in the US where airlines have substantial market power that generates profitability, whereas on other routes the opposite is true. He also noted that the ownership shares of investors in air carriers have changed over time. Therefore, any empirical study would have to consider two factors: 1) the change in the ownership of shares and 2) the change in competitive conditions in the industry, including whether LCCs and ultra-LCCs are competing with each other.

He concluded by noting that in his views there is no obvious mechanism or control relationship to draw conclusions on the competition impacts of common ownership. However, he did suggest the possibility that there could be some form of tacit coordination stemming from the oligopolistic nature of the airline industry, which at the same time can also generate benefits from the growth of large networks. Whether eliminating the oligopolistic structure of the airline would leave consumers better off is not, in his view, clear.

Next, the Chair gave the floor to Ms. Barbara Novick, the vice-president of BlackRock Investment Management LLC, to present a view from the asset management industry. Ms. Novick started by clarifying the role of asset managers, as some of the literature on common ownership conflates asset managers and asset owners in her view. She underlined that asset managers are fiduciaries, operating under an agency business model on behalf of clients, whom they call asset owners, such as pensions, insurance companies, sovereign wealth funds, or individuals. For example, while BlackRock manages \$6 trillion, that does not mean that BlackRock owns any of those assets. In fact, BlackRock owns none of those assets. Since assets under management (AUM) belong to clients, the investment results belong to the client.

Ms Novick also highlighted that BlackRock manages thousands of portfolios, each of which comes with a specific mandate that can be extremely different from the others. Some

portfolios are ‘collective investment vehicles’, such as mutual funds, and many of the assets managed by BlackRock are held in separate accounts. For example, if a pension plan or a sovereign wealth fund gives BlackRock a mandate to manage assets on their behalf, the assets will stay on the balance sheet of the asset owner. Ms. Novick underlined that it is important to be aware of this relationship in order to understand that there is no incentive in her view to bring about anticompetitive effects.

When seeking to understand the impact of common ownership on incentives to compete, Ms. Novick emphasized the importance of understanding that asset managers are regulated both at the company and at the product level. Some of the regulations specify that fiduciary duty includes voting the shares of the companies they manage. In this context she also explained the concept of investment stewardship. Asset managers need to decide whether to make voting decisions themselves or outsource this function to a proxy advisory firm. Over the past decade, many clients encouraged asset managers to vote their proxies and to become more active as fiduciaries and asset managers. BlackRock has a global team of over 30 investment stewardship professionals which are considered actively engaged, but not activist investors, with a focus on the long-term rather than short-term profits.

In terms of their engagement priorities, Ms. Novick stated that BlackRock focuses on issues of governance, long-term corporate objectives, compensation, climate risk disclosure and human capital. As evidenced in voting statistics, BlackRock does not consistently vote with or against management. She stressed that BlackRock is independent and transparent in its engagement: it publishes its voting guidelines, engagement priorities, communications with CEOs and annual voting record, and it reports quarterly on engagement and voting activities. Investment stewardship activities do not include any discussion on product development or product pricing of the companies in question.

Another area of confusion, in her view, is threshold reporting. Institutional investors are required by many jurisdictions to report the shares they control, regardless of what type of portfolio is involved (e.g. separate accounts or commingled funds) and the type of investment strategy (i.e. active or passive). However, the reporting threshold is a regulatory concept, that does not reflect economic interests or differences across portfolios. Ms. Novick also emphasised that, while BlackRock is voting the proxies for the shares it manages, it has no economic interest in these companies. Ms. Novick also clarified the question of outsourcing of proxy advisory. As the German Monopolies Commission observed, there are some concentrations of voting rights. She noted that BlackRock estimates that proxy advisory firms are estimated to effectively determine between 10% and 25% of the votes in company meetings, depending on the investor base and company size .

Finally, Ms. Novick referred to the difference between asset owners and asset managers. BlackRock is an asset manager. Asset owners usually select a small number of companies to invest in, and part of that investment can include a requirement for a board seat. In contrast, BlackRock as an asset manager has no board seats. She stressed that BlackRock does not have an economic incentive to discourage competition. For example, with reference to the airline industry which was mentioned before, airline companies represent less than 1% of any major stock indices, but 99% of the companies in these indices may use airlines as part of their cost function, which raises the question of why any common owner would have an incentive to raise the cost on a small percentage of companies, when the remaining portfolio firms would be harmed by increased cost.

Ms. Novick concluded that the theories behind common ownership are certainly novel and provocative ones, but can be discounted based on an understanding of how the asset

management industry works. She noted that additional papers cast doubt on the assumptions, methodology and conclusions of papers that find common ownership can affect the degree and intensity of competition on markets. Ms Novick concluded that the academic debate on whether common ownership by asset managers lessens competition is far from settled, and that any analysis will need to factor in the roles of proxy advisory firms and compensation consultants before any conclusions can be drawn.

The **Chair** noted the disagreement among panellists regarding the conclusions of the empirical studies on the effects of common ownership, and emphasised that the roundtable is intended to introduce the debate rather than resolve the questions definitively. Then, he asked Professor Schmalz to react to the presentations and the remarks so far.

First, **Professor Schmalz** noted that since mutual funds charge a percentage of the value of the assets they manage, the asset value increases when competition decreases, so the incentives of investors are in his view aligned with the ultimate owners of this stock. With regard to the shareholdings in suppliers and customers, Professor Schmalz underlined that he does not think that a company would charge lower prices to all of its clients just because it has an interest in one of the clients. Vertical common ownership exists, but there is no theory that says that this would contradict anticompetitive effects of common ownership or horizontal shareholdings. In addition, he recognised that portfolio heterogeneity exists, but it appears that large investment managers do not vote differently in different portfolios, suggesting that such heterogeneity does not affect voting decisions.

## 2. Views of the delegations

Moving to the country contributions, the Chair turned to **Slovenia** to describe the authority's recent review of a transaction involving the sovereign wealth fund investing in multiple firms within an industry. Slovenia explained that the two largest asset management funds in Slovenia are entirely owned by the State and are entitled to manage the capital assets of the State in many firms. One fund was established to run the second pillar pension scheme, while the other one was established to manage the ownership interests of the State in over a hundred companies. The funds participate in general meetings of these firms; they also nominate their representatives on the supervisory boards. From a competition point of view, these funds together with the State represent a single economic unit, so the sum of the ownership in each company equals to the sum of the stakes of these two funds plus the stake of the State as well.

The Slovenian Competition Authority has recently received a merger notification involving these two funds and another foreign fund acquiring joint control over the largest company in the hotel accommodation services and spas markets. The analysis indicated that the acquirers have many corporate links, including minority shareholdings in competitors of the target company with interests ranging from 16 to over 40%. The acquirers also appointed representatives on the supervisory boards of some of the target company's competitors. Moreover, the analysis also indicated the presence of interlocking directorships which could lead not only to co-ordinated but also to unilateral effects. Slovenia noted that the parties proposed behavioural remedies to address these concerns but the case is still ongoing.

**Mexico** explained how the Federal Telecommunications Institute (IFT) analyses the degree of influence held by a common investor in competing firms, and specifically, how "significant influence" is defined. Mexico started by noting that it is common in the

telecommunications and broadcasting sectors in Mexico for institutional investors to hold shares in publicly listed companies. Common ownership by institutional investors was relevant in the analysis of some merger cases. In recent decisions, the IFT has considered significant influence as: the ability of an economic agent to participate or intervene in a significant way, directly or indirectly, by any means in decisions regarding the administration of the company as well as the definition of policies and management. This analysis is carried out on a case-by-case basis, and the IFT uses certain indicators to identify the ability to influence, such as 1) the ability or the right to designate or remove a member of the board or an important director or manager, 2) the percentage of voting shares owned - IFT uses a 10% benchmark for influence and 3) the framework for governance, accountability and investment practices of the investors.

Mexico indicated that international practise recognises there is a high risk of coordination when there are structural links between economic agents that compete in one or various markets. In order to assess this risk, the IFT looks at the market structure and its degree of concentration, and at the financial interests that this structural link represents for each of the parties. The IFT also analyses if the structural link still allows the parties to act independently. The IFT looked at several mergers involving common ownership, but none of these cases led to a conclusion of harm to competition, mainly because common institutional investors did not have the right to designate, remove or veto any of the members of the board, directors or managers. One case, a transaction between owners of television channels, was cleared with conditions. The IFT considered the level of market concentration, the presence of multi-market contacts, the low number of competitors in the markets, the common shareholders, and the existence of entry barriers in this case.

**Portugal** shared its experience with common ownership and the creation of a Central Register of Beneficial Ownership. In Portugal, a recent merger case called for an adjustment to the toolbox for assessing the competitive effects of mergers. The vertical merger involved the acquisition of the payment acquiring services business of UNICRE by SIBS, a quasi-monopolist in payment processing services. The parties displayed a high degree of common ownership and the transaction would create an additional minority ownership link. The effect of the minority shareholding acquisition would not be captured by a standard HHI, hence Portugal decided to use the modified HHI to assess the competitive impact of the merger. Portugal also relied on a merger simulation, in which they captured the vertical aspects of common ownership and the two-sidedness of the market, to estimate the impact of the merger on pricing incentives. Regarding the vertical aspects, the authority found that, due to common ownership, the banks had their incentives aligned to use the payment processor to exclude outside entrants to the market.

Finally Portugal highlighted that the beneficial owner central register, which entered into force in November 2017, gives information about the ownership of all the companies that are registered directly or indirectly via third parties. The register can be used not just to map out all the shareholders of each of the companies, but also to identify potential gun-jumping cases, because the changes need to be notified, and there is a penalty for not notifying these changes.

The Chair then turned to **Brazil** and asked for an explanation of the standards they apply in mergers filed by institutional investors. The Brazilian Competition Agency (CADE) explained that when the acquisitions do not reach the minimum acquisition threshold of 20% of shares, CADE typically does not investigate the presence of a common institutional investor. In addition, CADE considers only direct acquisitions among competitors and excludes those carried out by common investors. However, CADE considered common

ownership in a merger case filed by the companies Kroton and Estácio, both active in the market of on-campus and distance-learning education in Brazil. The merger was blocked due to the competitive risks raised in the on-campus segment by a common investor of the parties, which held minority shares in each of the companies. Prior to the notification of the transaction, the institutional investor voted in favour of the merger at the general assembly of shareholders of both competitors despite having a clear interest in the merger.

From a competition perspective, the case is an important indication of how an institutional investor can possibly exercise significant influence in decision-making processes involving competitive matters, which may have the potential to harm competition. However, with the exception of this case, the analysis of common ownership by institutional investors has not been the subject of deeper discussion by CADE. This may change in the future considering the increased capital market activities in Brazil.

Next, **Argentina** explained the analysis of common ownership in recent mergers in the telecommunications and oil and gas sectors. The acquisition of interests of Telefonica from Spain in Telecom Italia involved the acquisition of minority shareholdings; however, the analysis revealed that these minority shareholdings provided the acquirer substantial influence in the target company. In this case, the parties offered remedies to keep the two corporate entities separate (Chinese walls). In the oil and gas case, the analysis of the authority led to the opposite result. The investors acquired shares that were not substantial enough to result in substantial influence. Argentina concluded that even if there is no substantial influence, minority shareholdings may facilitate collusion and can be a factor to take into account when analysing the effects of a merger.

### 3. Possible solutions from law enforcement and regulatory perspective

The final part of the discussion dealt with possible solutions to the concerns associated with common ownership in terms of competition law enforcement and market regulation. The Chair gave the floor to the experts – Professor Elhauge, Professor Schmalz, Professor Rubinfeld and Dr. O’Brien – then to the EU and the US. Finally, Ms. Novick closed the discussion with an industry perspective.

According to **Professor Elhauge** the question is whether we can tackle potential problems with common ownership under the existing legal framework. In his view, the US legislation (the Clayton Act) is well-placed to deal with the problem. It blocks any stock acquisition that is likely to have anti-competitive effects, and does not require the acquisition of control or even of influence. The passive investor exemption (i.e. the investment-only exemption), is not in his view an obstacle for two reasons. First, this exemption only applies if the transaction is solely for investment purposes, meaning that the investor has no influence or voting rights, which is very unlikely for these kinds of cases. Second, even if a stock acquisition were solely for investment, that would merely change the standard of proof by requiring evidence on the actual or potential anticompetitive effects. In Professor Elhauge’s views, these cases should be investigated if 1) the horizontal shareholding level is high and 2) the transaction takes place in a concentrated market.

He also noted that these concerns can also be captured under the Sherman Act, according to which any ‘contract, combination in the form of trust or otherwise, or conspiracy’, in restraint of trade is illegal. Horizontal shareholding falls, in Professor Elhauge’s view, within the reach of this statute, since it involves contracts between corporations and common investors that give horizontal shareholders rights to vote and financial rights. He

also noted that, historically, the reason why, in the US, competition law is called antitrust is because it is aimed at prohibiting trusts that in fact were horizontal shareholders. The primary difference with the historical trusts is that the possible efficiencies of modern horizontal shareholding make it subject to rule of reason analysis, rather than to per se condemnation. Multiple minority horizontal shareholdings create aggregated anticompetitive effects, similarly to cases that involve exclusive dealing and vertical price fixing.

In terms of the applicability of EU competition law, Professor Elhauge observed that the EU merger control rules are undeniably narrower than the Clayton Act, but they can cover stock acquisitions that give a group of shareholders de facto control if they have collective decisive influence. He conceded that applying the EU merger regulation to ordinary horizontal shareholding would require some changes in EU enforcement practice, which has so far focused on cases in which more direct links among shareholders create the joint control. But he argued that the regulation could sensibly be interpreted to extend to cases without such direct links, just as the old merger regulation was interpreted to extend to cases of collective dominance without direct links between firms. The best argument against such an interpretation, he reasoned, was that other EU competition laws might offer a better solution, given that even such an interpretation of the EU merger regulation would still fail to fully address the horizontal shareholding problem, because the anticompetitive effects of horizontal shareholding do not depend on a showing that some set of horizontal stock acquisitions changed control by giving collective decisive influence over business activities to the horizontal shareholders.

A more promising avenue, according to Professor Elhauge, is to apply Article 101 of the EU Treaty, which covers agreements or concerted practices between undertakings that have the effect of restricting competition. For example, in the Philip Morris case, the European Court of Justice already held Article 101 covers minority stock acquisitions if they have the “effect of influencing anticompetitive behaviour”. Further, Article 101 covers concerted practices extending beyond agreements and thus includes any indirect contact having the effect of influencing the conduct of a competitor. Horizontal shareholding can be viewed essentially as an indirect contact that has the effect of influencing behaviour among competitors.

Lastly, he pointed to another aspect of EU competition law that is broader than US competition law. Article 102 covers not just single firm dominance, but also collective dominance, and one of the abuses covered is excessive pricing. He noted that the ban on excessive pricing is often not enforced, because the “excessive” price is hard to define for a monopolist or to avoid for an oligopoly, but also because monopoly pricing is a desirable reward for firms that have invested and won the competitive race. However, unlike monopoly or oligopoly pricing, horizontal shareholdings do not present these same difficulties. When horizontal shareholding anticompetitively increases the profits of the involved firms, it can be banned without requiring courts to define the acceptable price level, and it is not a desirable reward for an additional investment that created better market options; rather, it creates a collective dominance based on contractual and structural links that results in excessive pricing. Finally, Professor Elhauge expressed scepticism that fiduciary duty would prevent horizontal shareholdings from having anticompetitive effects, since anticompetitive pricing increases the profits of all firms in an industry, including the non-horizontal shareholders.

Then, **Professor Schmalz** was asked by the Chair to present some other policy proposals made in response to common ownership concerns. Posner, Scott Morton and Weyl

proposed that if an investor holds less than 1% of competitors, there is no presumed influence and such investors can index invest unrestrictedly. Professor Schmalz noted that the largest index fund in the world holds less than 1% of the US stock market. But if an investor is larger than that (including a fund family that de facto coordinates and centralises voting), it would essentially be required to pick one firm per industry. In theory, this proposal could be very attractive, because it gives large benefits for consumers and ordinary households by restoring firms' incentives to compete. In addition, Professor Schmalz noted that proponents of this approach argue that having more concentrated holdings in fewer firms gives better incentives to improve corporate governance.

Professor Schmalz indicated that there have been several critiques of the proposal. In his view, however, policy makers should keep in mind that the vast majority of households gain more from reduced consumer prices than from higher equity portfolio values, because most people do not have a large equity portfolio compared to their consumption basket. Although the proposal is likely to restrict the institutions' ability to diversify, it does not restrict households, who could still purchase several funds. Regarding the concern that the common ownership problem threatens index funds, he opined that addressing anticompetitive effects of common ownership does not imply destroying index funds, and that common ownership can be more pronounced with actively-managed funds, or index funds that are concentrated on a particular industry. Authorities can investigate common ownership by active mutual funds, hedge funds, or new-style private equity funds, and they can restrict or monitor the centralization of voting power across funds, all without touching on the business model of index funds. Thus, policies seeking to constrain common ownership could in fact encourage greater diversification across industries, and should not interfere with index funds.

The Chair then gave the floor to **Professor Rubinfeld** who began by saying that in the current US environment, institutional investors play a positive role in terms of their involvement through proxy voting. Thus, any policy move that prejudges the current situation and moves towards solutions that do not provide an opportunity for investors to participate would not be advisable. Without compelling evidence, radical policy changes should not be considered. In particular, the empirical work on the airline industry fails to deal with the specific structural features of the industry. Once a better understanding of the structure of the industry is developed, it may be more likely that the effects observed in empirical studies are attributable more to market power rather than common ownership. Professor Rubinfeld opined that policy recommendations should not detract from supporting the growth of index funds.

With respect to the legal arguments made by Professor Elhauge that cases could be prosecuted under section 7 of the Clayton Act, Professor Rubinfeld noted it is certainly a possibility, but cases would not likely be successful given the burden of proof. It would be particularly challenging when there is no clear evidence of control, such as an investor's representation on the board of directors. With regard to the possibility of pursuing a claim on Section 1 of the Sherman Act or Article 101 of the TFEU, he noted that in the absence of clear evidence of an agreement, neither possibility is likely. He concluded by mentioning that there is a risk of introducing aggressive solutions too early.

The **United States** was asked by the Chair to react to some of the risks identified in relation to the proposed measures on common ownership. According to the United States, interlocking directorates and cross-ownership by competitors where a possible coordination or control mechanism is clear are already covered by the US antitrust laws and both antitrust agencies have been active in this area. Turning to the question of common

ownership the delegate noted how economics has played an increasing role of antitrust law. Economic scholarship, for example, drove changes to the legal treatment of vertical restraints, as well as adjustments to the market share thresholds in the horizontal merger guidelines. Thus, agencies must be aware of the evolving scholarship, including in the area of common ownership.

However, the United States underlined that empiricism is the foundation of good policy in antitrust. This requires a better understanding of the mechanism through which common ownership would reduce competition. In addition, antitrust applies across all industries, which raises the question of whether these effects can be found outside the two industries – airlines and banks - that have been studied, and whether there is a scientific method that can be used to replicate these studies. It is also not clear whether there are certain firms or unique market conditions that are creating the observed effects. Going back to empiricism, the delegate noted that a much more robust understanding of the cause, the effect and the replicability across all industries are needed to change antitrust law in response to new and interesting theories - especially since it could have a negative impact on consumers' investments and ability to diversify. The US concluded that given the ongoing academic research and debate, and its early stage of development, the US was not prepared at this time to make any changes to its enforcement practices, but would consider enforcement actions where sufficient evidence exists that the effect of particular acquisitions may be substantially to lessen competition. The Chair asked **Dr. O'Brien** to share his views on possible uses of the modified HHI as a safe harbour for investors. Dr. O'Brien proposed distinguishing the question of policy in response to common ownership based on macro and micro levels. The macro level relates to the need for policy change towards minority shareholding. In his view, neither theory nor evidence at this point supports macro-level changes towards minority shareholdings, because it is not clear how minority shareholdings translate into control, and how institutional investors would have incentives to take anticompetitive actions even if they did have control. Similarly, it is not clear in his view how management compensation would lead to anticompetitive effects.

Dr. O'Brien cautioned against assuming that firms' incentives to raise prices increase with partial ownership of competitors. Rather, such an outcome only occurs in the economic literature under certain control assumptions, which are key in Dr. O'Brien's view. He also warned that decisions of competition authorities based on MHHI would be inconsistent with established safe harbour thresholds that are based on the HHI. He also argued that any merger investigation that analyses common ownership should measure it relative to the average in the economy, in order to support any concern about common ownership being particularly problematic in a given case.

Turning to the micro-level, he opined that efforts to account for common ownership using the MHHI and the pricing pressure index introduced ten years ago are valid, provided the control assumptions are clear. For example, if Firm 1 controls Firm A and acquires a financial interest in Firm B, which is its competitor, it can be expected that Firm 1 would take into account its partial ownership of Firm B in its decision making with respect to Firm A. A second example would be the cases where a firm has a clear controlling owner, even if financial interests are dispersed (i.e. a firm acquires a controlling interest and the majority of the voting shares, but only has a minority financial interest). He emphasised that, in such cases where you control two competing firms but have only a minority financial interest in one, the effects could be particularly harmful. Dr. O'Brien emphasised that understanding these patterns of ownership requires a case-by-case analysis.

Dr. O'Brien concluded that it needs to be clear what kind of influence common owners can exert, whether this influence is generating benefits or harm, and whether it is internalising common ownership in a way that is anticompetitive. He then emphasised that there is no one-size-fits-all analysis, and noted that while the discussion had not covered the topic in depth, if common ownership facilitates collusion, this should certainly be taken into account.

The Chair then gave the floor to Ms. Novick to present her thoughts on the proposed measures. While a manager of an active portfolio can choose to sell the securities of a company that has had poor performance or no longer fits the investment thesis, an index manager holds all of the companies in the relevant index and the manager cannot express its disapproval by selling the companies' stock. As a result, the fiduciary responsibility to engage and vote is more important than ever. With regard to the proposal to limit ownership, whether by limiting to 1% per company, or to a single company per industry, Ms. Novick noted that these policy measures could be applied to any large asset manager, or for that matter to large diversified asset owners who manage assets internally. This would include many large pension plans and sovereign wealth funds. She argued in particular that these proposals would negate the concept of an index fund, since index funds mimic the benchmark and the holdings in the benchmark. Index funds provide long-term patient capital to thousands of companies. The holders of index funds include institutions, as well as individuals, who can purchase funds directly, or hold them via a defined contribution pension plan. As a result, millions of individuals across the socio-economic strata are likely to invest some money in index funds. The proposed remedy would eliminate the benefits of diversification in any concentrated industries. She emphasised the need for investors to be able to diversify within industries, as well as across industries. Moreover, it would not be clear who could decide which single firm each investment fund could hold in each concentrated industry. Likewise, it is not clear how firms would ration stocks within the 1% limit across different portfolios, if the limit applies on a fund manager level. Ms. Novick noted that it is well known that a large sovereign wealth fund directly owns approximately 2.5% of every public company in Europe. Given that this asset owner uses an index approach, the 1% limit on holdings in companies in concentrated industries would pose an immediate problem for this investor as well as for many other investors. In addition, the allocation of capital today is across all industries, regions and capitalisations, whereas the proposed rules would cause allocations to be very targeted, which will be very harmful to the issuers.

In relation to a proposed policy that would not allow managers to vote proxies or engage with the companies in these concentrated industries, she noted that it is in direct contradiction with recent regulatory efforts that are encouraging entities to become more engaged in corporate governance. She noted that, in the OECD, there is a group focusing on corporate engagement, and in the EU, the shareholder's rights directive actively encourages asset managers and asset owners to engage with companies on long-term performance and environmental, social and governance (ESG) criteria. In the UK, asset managers are encouraged to become signatories to the financial reporting council's UK stewardship code. There are similar codes in Japan and the Netherlands, which most asset managers have agreed to. Further, the investor's stewardship group, which includes both public sector and private sector entities, has also issued a stewardship framework for institutional investors and corporate governance principles for US-listed companies. Participants in that group include several entities that have been leaders in corporate governance and ESG matters. As public authorities are actively debating how to get asset

managers to be more vocal on ESG issues, it would seem odd to recommend restricting corporate engagement or disallowing proxy voting.

Ms. Novick continued by highlighting that asset managers lack the incentive to reduce competition in any concentrated industry or in any industry at all. Common ownership by a direct investor is a different matter, as they have board seats, and direct economic interest in the companies that they own, whereas an asset manager is acting on an agency basis. She also expressed the view that there is no compelling causal link in any of the literature and no evidence of any link between common ownership and consumer harm. However, since policy measures have been proposed, it is important to consider the impact these measures would have. Specifically, harms to both the companies who are issuers and to the investor, which include many small investors who are not just consumers of products, but are also investors, often in index funds.

She then noted that various countries already have antitrust remedies that would have been implemented if there was a particular problem in a specific industry. Thus, in Ms. Novick's view, there is no need for further measures, for example those limiting funds to investing in one firm per sector, or those preventing investors from voting.

Finally, Ms. Novick highlighted what are, in her view, critical omissions in the original papers on common ownership. In particular, she noted that (i) the paper on executive compensation fails to account for the role played by compensation consultants to public company boards, (ii) all of the papers fail to address the role of proxy advisory firms who influence more votes than any individual asset manager (where proxy advisors are estimated to control or influence between 10% and 25% of various votes). In addition, Ms. Novick indicated that the original papers on common ownership conflate asset owners and asset managers. She illustrated the difference using the example of an asset owner who holds board seats which is fundamentally different than the agency model of an asset manager. These details reflect the importance of bringing practitioners' voices into the discussion to fill in the gaps of a theoretical econometric model.

The European Commission then took the floor, specifically to discuss the statement from Professor O'Brien about basing competition authority decisions on the MHHI. The European Commission insisted that its Decision related to the merger between Dow and DuPont, referred to by Professor O'Brien, had a full annex devoted to this issue, which (i) reported facts on the extent of the common ownership in this industry, (ii) documented the fact that large minority shareholders have more influence than their equity share, (iii) described the specific relationship between the Parties and their large shareholders, then (iv) summarized the economic literature and then (v) looked into the possible way to factor in the existence of common ownership through MHHI. The European Commission also made clear that its Decision recognized the challenges of this topic, in particular the assumptions on control necessary to compute MHHI, and therefore did not derive any conclusions on the basis of MHHI levels. The representative of the European Commission ended his intervention by reading the last paragraph of the annex which states: "Based thereupon, the Commission considers that, in general, market shares used by the Commission for the purpose of the assessment of the Transaction tend to underestimate the concentration of the market structure and, thus, the market power of the Parties, and that common shareholding in the agrochemical industry is to be taken as an element of context in the appreciation of any significant impediment to effective competition that is raised in the Decision.

#### 4. Conclusions by the Chair

Finally, the **Chair** concluded the Hearing by summarising some of the main points emerging from the discussion. First, he highlighted one of the key questions raised by Dr. O'Brien: "*do we have an easy understanding of how a minority shareholding can transform itself into control?*" He continued by noting that the battle over the empirical results can be hard to interpret for antitrust agencies, and may at this stage simply require the recognition that there is substantial controversy. On the potential for the creative use of antitrust, the Chair noted that antitrust authorities are under the purview of courts, and courts tend to be fairly conservative when assessing economic evidence. Courts, for predictability and legal security reasons, prefer to have well-established theory and limited controversy over the basics of the empirical studies. Thus, the creative use of existing antitrust provisions is likely to be more of an academic exercise than a likely outcome. It is therefore not clear, in the Chair's view, that the instruments competition authorities have are necessarily able to resolve competition concerns, assuming that there is an antitrust problem.

In terms of the policy proposals discussed, the Chair noted that they are more in the purview of legislators rather than of competition agencies. It is important to note that these proposals may have some unintended and detrimental consequences to the industry. He observed that there was consensus that competition policy should not aim to destroy institutional investment business models, but more to explore whether there is a competition problem of sufficient importance and to understand how to handle it. To conclude, he highlighted that the discussion has covered many aspects of the topic and benefitted a great deal from the different perspectives of the panellists and from the country contributions.