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Spanish banks fined for PF derivatives fixing

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The Spanish antitrust authority has punished four domestic lenders. Project finance loan derivatives are at the heart of the case. By **Stefano Berra**

Spanish antitrust authority CNMC has fined CaixaBank, Santander, BBVA and Sabadell €91m in total for allegedly fixing interest rate derivatives for project finance customers.

The CNMC said the banks arranged swaps and floor hedging instruments “behind the back” of the borrowers, on terms different from those initially agreed under market conditions. It said the behaviour lasted between 2006 and 2016 and amounted to a “very serious infraction” of Spanish and European antitrust laws.

CaixaBank received the largest fine of €31.8m, followed by Santander with €23.9m, BBVA with €19.8m and Sabadell with €15.5m.

Santander and BBVA told PFI they would appeal the decision. A spokesperson for Santander said “the bank believes it acted correctly and in line with market standards”.

CaixaBank and Sabadell did not respond to a request for comment but are reportedly looking to appeal too. The banks can file an appeal of first instance at the Audiencia Nacional – Spain’s High Court – within two months.

Santander is being advised in the matter by Linklaters, BBVA is being advised by Ramon y Cajal, CaixaBank by Hogan Lovells and Sabadell by Roca Junyent.

While the size of the fines is limited, the decision might leave the banks exposed to the possibility of action for damages by clients, particularly if the judgement is confirmed on appeal.

The CNMC’s decision covers a period of 10 years during which a large number of project financings were signed by the four lenders, including large deals done before the country’s economic crisis. The fine could set a precedent for other lenders that might follow similar derivatives business practices.

The CNMC launched the investigation following complaints by wind farm developer Vapat, described by the authority as one of Spain’s ten largest wind power operators.

The company is led by Rafael Gonzalez-Vallinas Delgado and has 472MW of wind capacity in the country. Gamesa operates 216MW of the company’s wind parks.

Vapat filed a complaint in June 2015, providing evidence from the financing of its wind farms held through SPVs Bajoz Eolica, Hornija Eolica, Esquilvent and CyL Energia Eolica.

Bajoz Eolica and Hornija Eolica were financed in 2010 with €81m by the four banks plus ICO. Esquilvent’s three wind farms in Palencia totalling 140.6MW were funded with €182.3m later in the same year. CyL Energia Eolica, which includes three wind farms in Burgos totalling 140.6MW, was financed in 2011 with €177m.

The authority expanded the scope of its investigation, looking into 43 project finance deals with 22 sponsors. During the investigation it requested emails and phone call recordings from the banks.

Among the other project financings examined are Parc Eolic Mudefer, Africana Energia, various deals of Renovalia Energia, Ibereolica Solar Moron, Ibereolica, Parque Eolico Cova da Serpe, Autoestrada Ourense Celanova Sociedade Concesionaria Da Xunta De Galicia, and Termosolar Borges. It also included some private hospital deals such as Clinicas del Sur and Palex Medical.

The authority’s decision focused on derivative products commonly applied to hedge interest rate changes in project finance deals, such as interest rate swaps to set a fixed interest rate for projects and cap-and-floor collars to set minimum and maximum rates.

The CNMC said the term sheets of Vapat’s wind financing deals compelled the borrower to sign interest rate hedging agreements with the same lenders providing the debt, covering a minimum amount and duration. The authority observed similar clauses in several of the other transactions it examined.

In Vapat’s case, the hedging took the shape of an interest rate collar, while many other deals were structured as swaps.

Vapat cancelled part of the swaps in 2012 after some of the debt was amortised, paying the relevant breaking cost.

At the time, the company commissioned an independent report that suggested derivative prices were inflated by as much as 100bp over market values – a figure disputed by the banks, according to the CNMC’s decision.

The banks confirmed that they agreed among themselves both debt margins and the floor in the collar contracts, according to the decision.

In the case of Esquilvent, one bank proposed a floor of 3.14%, accepted by the others, before financial close. A similar process took place in the other financings.

The CNMC refrained from saying it was illegal for banks to agree on the same pricing in a deal, whether for debt margins or derivatives pricing. This is allowed under competition law as a condition necessary to the functioning of the syndicated loans market.

However, the authority chastised the banks for agreeing higher prices among themselves and “behind the back and with total ignorance of the client”, often justifying it with the borrowers with market volatility, after having initially offered lower pricing to win business.

The banks said conversations were only intended to establish there were the right conditions to sign the deals. They argued it was legitimate practice for the banks to present a joint offer.

The lenders pointed to a report by the Bank of Spain that says credit syndication and joint pricing for the derivatives linked to loans is a legitimate business practice.

CaixaBank lamented that the decision was partly based on “unfortunate telephone conversations in relation to two operations” and “unfortunate jokes between two operators”.

The CNMC said that even if banks were allowed to offer a joint price, they needed to offer the best market price and the process needed to be more transparent.

The authority said there were “radically different” dynamics between the banks’ initial autonomous offers, described as transparent and without collusion, and the following joint offer, which were more expensive for the clients.

It said it was unjustified to force borrowers to sign derivatives with the same banks providing the underlying project finance loans.

The decision could have far-reaching implications for the Spanish project finance market as it returns to growth with new greenfield renewable power and infrastructure deals after years of subdued activity.

However, it remains to be seen whether it will survive an appeal. Some antitrust lawyers have expressed doubts as to whether the behaviour was a violation of competition law.

Pedro Callol, an antitrust lawyer at Callol Coca & Asociados in Madrid, said the decision scrutinises the manner in which the joint selling is taking place, allegedly exploiting an information asymmetry between lenders and borrowers and resulting in a price above the market price.

“It seems the CNMC wished to avoid the ‘hot potato’ of having to decide on whether syndicated loans and their ancillary derivative products are justified as a form of joint selling,” he said.

“The decision relies on the fact that an information asymmetry has been exploited, though the doubt arises as to whether civil law, consumer protection – noting that, in this case, the customers are companies, not consumers – or financial regulation would not be better suited to address the concerns.”

Other countries could follow the example of Spain in examining price-fixing practices. At the European level there is a growing regulatory interest in the way banks cooperate in the syndicated loans market. In the past the Dutch Competition Authority and the UK Financial Conduct Authority looked into the matter.

Last April, the European Commission launched a tender to commission a study into syndicated lending. While the study is characterised as a general market study, more in-depth investigations might follow.