

McCann FitzGerald

Competition Authority Seminar

Control Sanctions – The EU
Perspective

*“Sleeping with the enemy”:
the morning-after options*

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Indicia of a cartel

A “*suspension of hostilities*” – in traditional international law, a truce in wartime used for the exchange of prisoners of war.

Now: an uneasy alliance between rivals – has been described as “*sleeping with the enemy*” to capture “*the ambiguous relationship of intimacy and hostility reflected when competitors become bedfellows for economic gain at the expense of the public.*” (Hardy & Joshua: “Regulatory Cartels in Europe”/Oxford University Press, 2003).

“*Hard core cartels*” – the most egregious form of antitrust violations (price-fixing, market allocation, bid-rigging).

“*[Cartels] serve to restrict competition without producing any objective countervailing benefits... companies participating in a cartel produce less and earn higher profits. Society and consumers pay the bill. Resources are misallocated and consumer welfare is reduced. It is therefore for good reasons that cartels are almost universally condemned.*” (Mario Monti, European Commissioner for Competition, September 2000).

An uneasy alliance

Inherently unstable – “*The problem with a cartel is cheats.*” (Posner)

Game Theory:

- competition results in low prices
- an effective agreement to collude results in high prices for all participants

BUT a given participant will gain market share by cheating (i.e., under-cutting others);

BUT if all do this, it will lead back to the low-price competitive outcome!

So, “... *while firms may have an incentive to collude, achieving and then sustaining a collusive outcome can be extremely difficult.*” (Bishop & Walker: “*Economics of Competitive Law*”. Sweet & Maxwell, 2002)

Hence the need for monitoring, policing, enforcing cartel rules, thereby increasing the risk of detection.

An uneasy alliance

The Prisoner's Dilemma:

Faced with a perceived high risk of detection and potentially severe penalties, the cartel participants' options are:

- (1) provide the authorities with the evidence that they need in exchange for immunity or a significantly reduced fine;
- (2) stay silent, in the hope that the other participants will do likewise, and that the authorities will be unable to prove their case.

The first option is the rational choice for each participant, assuming he has no concerns about the impact on other participants. But success will depend on getting in first (or at least early).

An uneasy alliance

The inherent instability of cartels has been exploited by competition law enforcers through the creation of incentives for the participants to break ranks. This has involved a combination of:

- significant penalties
- effective, flexible immunity/leniency programmes.

Outstandingly successful in the US. Increasingly successful in the EU.

Risk of Detection

Risk of risk of detection may come from various sources:

- competition agency investigation;
- complaints by customers, competitors, employees (including ex-employees);
- other cartel participants (including leniency applicants).

Detection: Initial reactions

Initial reactions vary, but the following are not uncommon:

- Denial:
 - *“no agreement”*
 - *“no effect on competition”*
- Justification:
 - *“necessary for survival – prices were unsustainable”*
- Blame:
 - *“we went along with it”*
 - *“we had to meet targets”*
- Followed by: Fear:
 - 10% of turnover!
 - prison (possible extradition risk)
 - other regulatory exposure damages (treble in the US), including class action suits

Eventually leading to: Risk assessment – and review of options

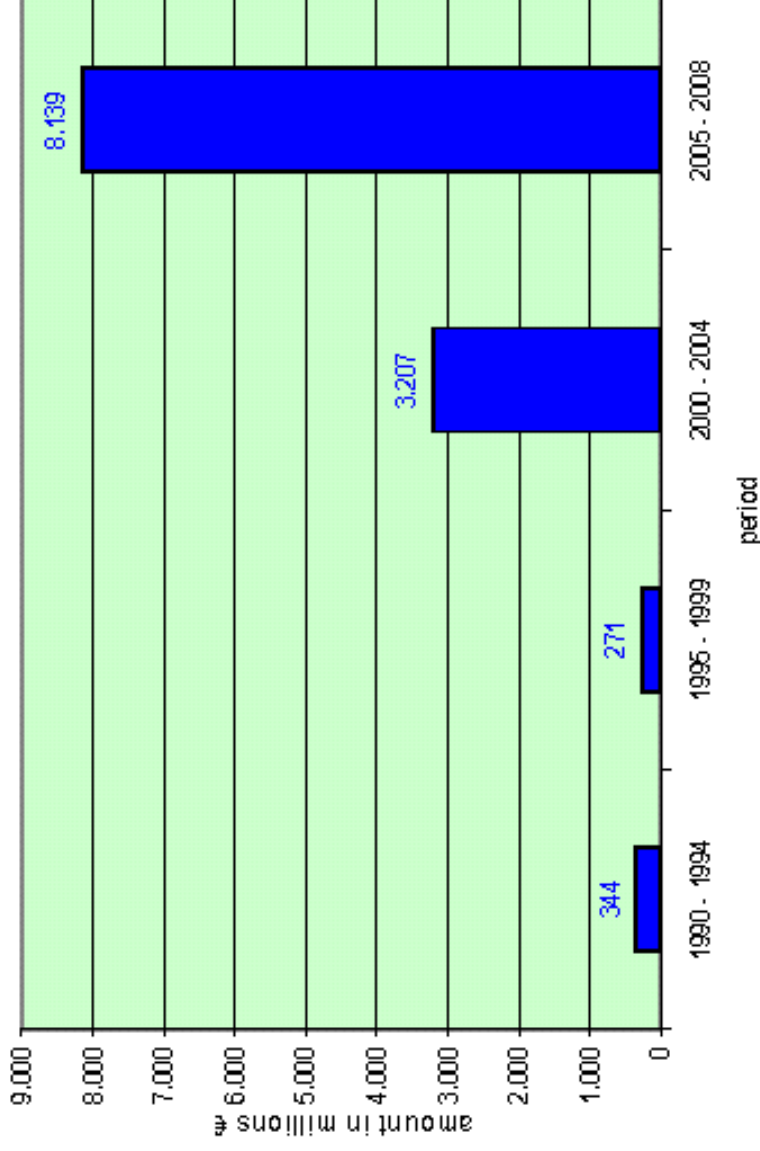
Risk Assessment – Severity of fines (1)

Some recent fines in EU cartel cases:

- 12.11.08: Four car glass producers fined €1.384 billion. St Gobain fined €896 million (including a 60% increase for recidivism).
- 15.10.08: two banana importers fined €60.3 million. A third, Chiquita, was granted full immunity.
- 1.10.08: Nine companies in the paraffin wax business fined €676 million. Shell received full immunity.

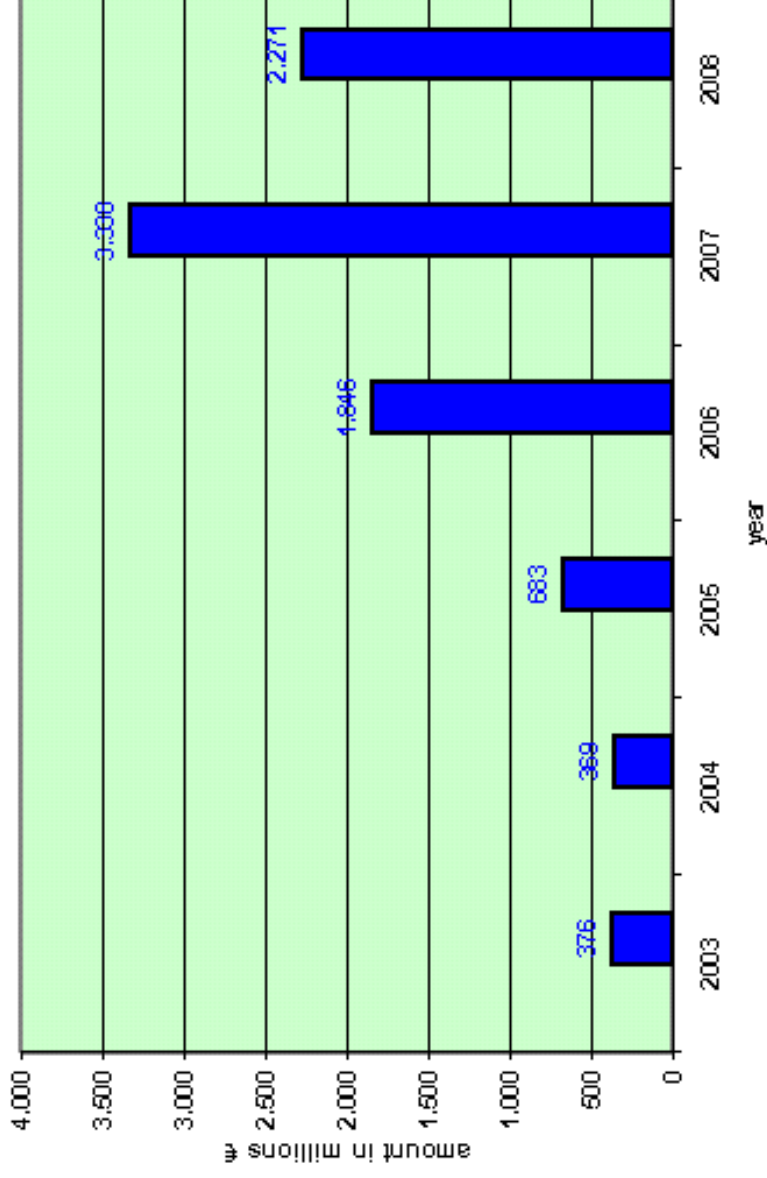
Risk Assessment – Severity of fines (2)

- Fines imposed (corrected for court judgments) period 1990-2008



Risk Assessment – Severity of fines (3)

- Fines imposed (corrected for court judgments) period 2003-2008



Risk Assessment – Severity of fines (4)

- Ten highest cartel fines per undertaking (since 1969)

Last update: 11 November 2008++

Year	Undertaking**	Case	Amount in €*
2008	Saint Gobain	Car glass	896.000.000
2007	ThyssenKrupp	Elevators and escalators	479.669.850
2001	F. Hoffmann-La Roche AG	Vitamins	462.000.000
2007	Siemens AG	Gas insulated switchgear	396.562.500
2008	Pilkington	Car glass	370.000.000
2008	Sasol Ltd	Candle waxes	318.200.000
2006	Eni SpA	Synthetic rubber	272.250.000
2002	Lafarge SA	Plasterboard	249.600.000
2001	BASF AG	Vitamins	236.845.000
2007	Otis	Elevators and escalators	224.932.950

* Amounts corrected for changes following judgments of the CJF and ECJ.

Risk Assessment – Severity of fines (5)

- Overall maximum: 10% of total turnover (Art 23(2), Regulation 1/2003)
- Fining Guidelines (2006):
Commission Press Release: “...companies involved in a long lasting infringement in a large market should be prepared to receive significantly higher fines than in the past.”
- According to one study (Veljanovski, 2007), some 98% of all fines imposed by the Commission between 1999 and 2007 have been appealed to the CFI, which has reduced them by an average of 19.3%. But that may be changing – the CFI has recently increased a fine imposed by the Commission.

Risk Assessment – Severity of fines (6)

Example of methodology:

- Basis: value of sales in relevant market (say, €100 million)
- Calculate basic amount of fine:
 - for gravity of infringement: up to 30% say, 25
 - for duration (e.g. 5 years): €25m x 5 125
 - “entry fee”: 15-25% of sales say, 25 150
- Adjust upwards (ring-leader; refusal to cooperate; repeat offender) e.g.: 2 x 150 300

Fine may also be increased further to ensure it exceeds gains improperly made and, for very large companies, to ensure a sufficient deterrent effect. (Subject, of course, to the overall limit of 10% of the undertaking’s total turnover in all markets.)

May also be reduced for some mitigating circumstances.

Risk Assessment – Other risks

- Criminal prosecution in certain Member States (including Ireland) and elsewhere, particularly the US.
- Private damage actions; a very significant factor in the US (treble damages, class actions); likely to become significant in Europe.
- Other regulatory exposure/sanctions (e.g., disqualification as a director; securities regulations; shareholder derivative actions; exclusion from government procurement).

The Process

- **Internal investigation**
 - by whom?
 - which jurisdictions?
 - implications for individuals in relevant jurisdictions; need for independent advice for employees?;
 - may be other reporting obligations (e.g. Sarbanes Oxley)
- **Conflict of Interest**
 - representation of parties
 - communication between parties/lawyers
- **Coordination across jurisdictions**
 - facts, exposure, options may differ radically



The Options

- Denial
- Seek immunity/leniency
- Settle

The Options - Denial

- Denial:
 - assess evidence and legal arguments (if any)
 - assess risk of detection
 - by Commission raids
 - through complaints (customers, employees)
 - through immunity/leniency applicants

Denial has become a much riskier option in recent years.

The Options – Seek immunity/leniency (1)

- Speed of the essence: only the first in will get full immunity; later applicants may get reduced fines
- Need for coordination across jurisdictions (especially those that criminalise cartel activity)
- Under the EU Programme:
 - (1) Immunity
 - application possible before or after an inspection
 - initial application may be on a hypothetical basis – if immunity not available, may withdraw
 - marker system – to protect the applicant’s place in the queue
 - not available for ring-leader
 - no disclosure to other participants
 - full disclosure of information; must be sufficient to enable Commission carry out an inspection or find an infringement
 - statements may be oral (to protect against discovery in civil proceedings)

Seek immunity/leniency (2)

- Under the EU Programme (cont'd):
 - (2) Reduced fines:
 - where immunity not available
 - evidence must represent “significant added value”
 - possible reductions:
 - first: 30-50%
 - second: 20-30%
 - subsequent: up to 20%
- Some dissatisfaction with the process:
 - lack of clarity about leniency reductions until the last minute
 - leniency discounts low or non-existent in some cases
 - Commission’s interpretation of “significant added value”

Settlement

- Very recent development.
- A mechanism for closing files
 - has obvious appeal for the Commission
 - will appeal to parties only where they believe their defence is weak and want to close the file
- There are concerns about how the process will work:
 - minimal fine reduction – described as an “anaemic carrot”
 - lack of transparency about final calculation
 - risk of Commission withdrawal at any stage
- But follow-on implications could be serious (e.g. criminal prosecution; damages actions).

Conclusions

- The 2006 Fining Guidelines and Leniency Notice have moved the goal posts – the incentives to seek immunity/leniency have significantly increased.
- There are concerns about the process followed by the Commission in relation to the reduction of fines which could have the effect of reducing the incentive to seek leniency and, in particular, to settle.
- The need for multi-jurisdictional applications remains a big challenge, but are essential if the collateral damage of disclosure is to be minimised.
- The moves towards greater coordination of national leniency programmes within the EU is to be welcomed.

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