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‘Criminal Sanctions for Cartel Activity – An International Perspective and Implications for Finland’

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Dr Peter Whelan
Associate Professor in Law
School of Law
University of Leeds

Aim and Layout of the Presentation



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✦ Aim:

To consider the desirability of introducing criminal cartel sanctions in Finland

Central argument: criminal cartel sanctions **should be introduced in Finland**

✦ Layout:

Part I: Introductory Comments

Part II: The Primary Justification: Deterrence Theory

Part III: Problematic Issues

Part IV: Specific Recommendations



- ✦ Cartel activity can be defined as:
 - ✦ the making or implementing of an anticompetitive **agreement**, anticompetitive **concerted practice**, or anticompetitive **arrangement** by competitors to **fix prices**, make **rigged bids** (collusive tenders), establish **output restrictions** or quotas, or **share or divide markets** by allocating customers, suppliers, territories, or lines of commerce (OECD)

- ✦ Common ground:
 - ✦ Cartels are (usually) damaging to the economy
 - ✦ Cartels should be prohibited to get max benefit from the free market
 - ✦ Adequate sanctions should exist to deter cartels

- ✦ Scope for disagreement:
 - ✦ What shape the 'adequate sanctions' should take
 - ✦ Central to the debate: issue of criminal sanctions (imprisonment)



- ✦ Central to the debate: **issue of criminal sanctions** (imprisonment)
- ✦ **European Commission** cannot impose criminal sanctions
- ✦ **Traditionally** within the EU, cartel enforcement has ‘been of a predominantly **administrative character**, and when penalties have been imposed these have, in legal terms, commonly been of an administrative or civil nature’ (Harding)
- ✦ Things have been **changing**:
 - ✦ OECD’s 2nd Cartel Report
 - ✦ US DoJ – advocates cartel criminalisation
 - ✦ Some EU jurisdictions have introduced criminal cartel sanctions (UK, Ireland, Denmark, Estonia...)
- ✦ A significant number of academics have **supported** these moves (Calvani, MacCulloch, Stephan, Werden, Wils...)

Part I: Introductory Comments



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Source: Stephan

- * Not just European issue: growth in cartel criminalisation globally
- * But custodial sanctions only imposed in 3 jurisdictions (Israel, UK and US)

Part II: The Primary Justification: Deterrence Theory



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- ✦ Deterrence theory: criminalisation can be justified on the basis that it leads to the **prevention of future** cartel activity
 - ✦ Central idea: punishment can be set at a level that causes individuals to decide that the activity is not in their interest
 - ✦ To deter: ensure the **cost** of activity outweighs its **expected benefit**

Punishment imposed > cartel profit/probability of punishment = deterrent
- ✦ **Primary justification** for criminal cartel sanctions is deterrence
 - ✦ Criminal sanctions are ‘the most meaningful deterrent to antitrust violations’ (Liman)
 - ✦ They ‘send a message to other business executives about the risks and penalties for this kind of behaviour’ (Bauer)
- ✦ Criminalisation argument involves the following steps:
 - (1) Determine the **size** of an effective **deterrent fine**
 - (2) Explain why one **cannot impose** that fine (ie that there is a deterrence gap)
 - (3) Explain how criminal sanctions **fill the deterrence gap**

Part II: The Primary Justification: Deterrence Theory



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(1) Determine the **size** of an effective **deterrent fine**

- ✦ A number of papers estimate the size of an effective deterrent
- ✦ **Wils** (in 2002 and 2005) estimated it at **150% of annual turnover**
 - ✦ 2002: [gain (10/2) = 5%] x [duration = 5 years] / [probability of detection = 1/6]
 - ✦ 2005: [gain (20/2) = 10%] X [duration = 5 years] / [probability of detection = 1/3]
- ✦ Calvani has also come to this figure
- ✦ Werden (in 2009) estimates the figure to be 200% of annual turnover
- ✦ Important to note:
 - ✦ Wils's figure does not contain rate of interest
 - ✦ The figures are **conservative** estimates:
 - ✦ Connor and Lande (600 cases)
 - ✦ average overcharges in EU were within 28 to 54%
 - ✦ average duration - 7 to 8 years
 - ✦ Bolotova and Connor (56 recent international cartels)
 - ✦ average duration of an international cartel – 6.6 years
 - ✦ median mark up was 27%

Part II: The Primary Justification: Deterrence Theory



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(1) Determine the **size** of an effective **deterrent fine**

- ✦ **Wils** (in 2002 and 2005) estimated it at **150% of annual turnover**
- ✦ This figure is a conservative estimate:
 - ✦ Combe and Monnier (2011):
 - ✦ Analysed 64 cartel decisions adopted by EC between 1975 and 2009
 - ✦ Average duration – 7 years (median was 5.6 years)
 - ✦ Smuda (2014):
 - ✦ Focused on 191 overcharge estimates
 - ✦ Mean overcharge – 20.7%
 - ✦ Median overcharge – 18.37
 - ✦ Average cartel duration – 8.35
 - ✦ Combe et al (2008):
 - ✦ Average rate of detection in any one year – 12.9 to 13.3%
- ✦ These studies would **increase** the effective fine beyond 150%

Part II: The Primary Justification: Deterrence Theory



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(2) Explain why one **cannot impose** the fine (ie there is a ‘deterrence gap’)

✦ (a) The firm will **not have actually received 150%** of annual turnover from the cartel – the fine is increased to take account of the rate of detection

✦ (b) The **profits** from the cartel may well have been ‘**spent**’ (taxes, dividends, salaries...)

✦ Risk: that the company will be forced into **liquidation** if the effective fine is imposed!

✦ This is unacceptable:

- ✦ Social costs
- ✦ Political fall out
- ✦ Concentration of the market

✦ Consequence: fines imposed on undertakings will achieve **under-deterrence**

Part II: The Primary Justification: Deterrence Theory



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(3) Explain how criminal sanctions fill the deterrence gap

- ✦ Including punishment **imposed on individuals** can improve deterrence:
 - ✦ Decisions to cartelise are taken by individuals
 - ✦ Need to ensure that their **own interest** is not served through cartel activity
- ✦ But that punishment should **not be merely financial**:
 - ✦ The firm can **indemnify** the individual (pay the fine)
 - ✦ Effectively this neutralises the advantages of individual (financial) punishment
- ✦ What is needed is punishment that **cannot be indemnified** by the firm
 - ✦ Custodial sentences cannot be indemnified
 - ✦ Reason: cartelists will not accept money to go to prison
 - ✦ Liman: 'For the purse-snatcher, a term of imprisonment may be little more unsettling than basic training in the army. **To the businessman, however, prison is the inferno, and conventional risk-reward analysis breaks down when the risk is jail.** The threat of imprisonment, therefore, remains the most meaningful deterrent to antitrust violations.'

Part II: The Primary Justification: Deterrence Theory



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✦ Summary of the deterrence-based argument:

- A fine of 150% of annual turnover is needed to deter an undertaking
- Such a **fine cannot be imposed** for practical reasons (e.g. liquidation of the company)
- Turn to **individual sanctions** to fill the deterrence gap
- However these sanctions must be more than mere monetary sanctions – otherwise indemnification will occur (i.e. firms will pay the fine)
- Custodial sanctions are **non-indemnifiable**
- In addition: custodial sanctions are also more condemnatory and more newsworthy than mere fines (which is important for deterrence)



- ✦ Cartel criminalisation is not without its **challenges**
- ✦ Three problematic issues are considered in turn here:
 - (a) Dealing with **legitimate cartel activity**
 - (b) Avoiding the negative impact of **Regulation 1/2003**
 - (c) Protecting the **administrative leniency** programme

(a) Dealing with **legitimate cartel activity**

- ✦ Unfortunately there is such a thing as ‘legitimate’ cartel activity
 - ✦ TFEU and Finnish law both provide ‘exceptions’ to their cartel prohibitions:
 - ✦ Examples: Article 101(3) TFEU; Section 6 of the Competition Act (No. 98/2011)
 - ✦ Often difficult to substantiate in practice, but legal possibility exists
 - ✦ OECD acknowledges this:
 - ✦ ‘the hard core cartel category does not include agreements, concerted practices, or arrangements that (i) are reasonably related to the lawful realisation of cost-reducing or output-enhancing efficiencies, (ii) are excluded directly or indirectly from the coverage of a Member country’s own laws, or (iii) are authorised in accordance with those laws’
- ✦ So using OECD definition for a criminal offence would be **too broad**
- ✦ Challenge: to capture **illegitimate cartel activity** and not criminalise legitimate cartel activity [main difficulty is (i) – ‘**efficiency defence**’]



(a) Dealing with **legitimate cartel activity**

- ✦ The main difficulty is how to deal with the ‘efficiency defence’
- ✦ One could simply provide an **express defence** like Article 101(3) TFEU
 - ✦ But it involves a form of **economic assessment**
 - ✦ Problematic:
 - ✦ (a) Forcing criminal courts to undertake complex economic analyses ‘runs counter to our notions of the relative **institutional competence** of criminal courts as compared with a specialized administrative agency’ (Warner and Trebilcock)
 - ✦ (b) it also injects a **degree of inconsistency** into the law, as it ‘leaves open the possibility of inconsistent findings between criminal and civil proceedings arising as a result of differences in economic judgement between a lay jury [or a non-specialised panel of criminal judges] and a specialist “civil” tribunal’ (Pickford)
- ✦ Some countries (eg Ireland) have efficiency defence; others do not



(a) Dealing with **legitimate cartel activity**

- ✦ To avoid problems what is needed is the carve out of 'acceptable' cartel activity **without requiring decision-maker** to conduct **economic** analyses
- ✦ Two ways: (i) creation of 'white list' of agreements (Australia); (ii) publication/notification carve out (UK)
 - ✦ (i) White Lists
 - ✦ *Approach*: certain agreements (defined **by type** rather than economic effects) are deemed outside of the criminal law
 - ✦ *Advantages*: limits the offence; provides some business certainty
 - ✦ *Disadvantages*:
 - ✦ Runs counter to current EU approach
 - ✦ Gives rise to interpretational difficulties
 - ✦ Inevitable that economic arguments will come in (to determine if agreement is of type allowed)

(a) Dealing with **legitimate cartel activity**

✦ (ii) Publication/notification carve out:

✦ *Approach:* provide circumstances in which criminal cartel offence will **not be committed** (not related to economic assessment)

- ✦ (a) public publication of agreement prior to implementation
- ✦ (b) notification of agreement to NCA prior to implementation

✦ *Disadvantages:*

- ✦ Places onus on cartel parties to take action to avoid criminal sanctions

✦ *Advantages:*

- ✦ Provides business certainty: easy to comply with
- ✦ Published/notified info does not need to be extensive
- ✦ Operationalises '**efficiency defence**' **without requiring economic analyses** by the criminal court:

- ✦ If after self-assessment cartelists believe agreement is 'legitimate', to avoid criminal sanctions they simply publish/notify₆

(b) Avoiding the negative impact of **Regulation 1/2003**

✦ If Regulation 1/2003 applies to the enforcement of the national cartel offence a number of problematic issues could arise:

✦ **(i) Article 35(1): designation**

- ✦ MS shall designate NCA(s) responsible for application of Articles 101 & 102
- ✦ Could mean criminal courts will need to be designated
- ✦ *R v. IB* – Court of Appeal did not agree; unsettled issue, but surmountable

✦ **(ii) Article 11(6): pre-emption by the Commission**

- ✦ The initiation by EC of proceedings for the adoption of a decision under Chapter III of Reg 1/2003 shall **relieve the NCAs** of their competence to apply Articles 101 & 102

✦ **(iii) Articles 3(1) and 3(2): convergence**

- ✦ If there is an effect on trade, NCA must also apply Article 101
- ✦ AND cannot allow for the application of the national cartel offence to result in a stricter prohibition of the cartel than that under Article 101
 - ✦ Argument: this could **introduce 'efficiency defence'** in through the backdoor



(b) Avoiding the negative impact of **Regulation 1/2003**

✦ **Interpretation 1 (UK OFT (now CMA)):**

✦ Focus on Recital 8 of Reg 1:

✦ Regulation 1/2003 'does not apply to national laws which impose criminal sanctions on natural persons except to the extent that such sanctions *are the means whereby competition rules applying to undertakings are enforced*'

✦ Idea: if criminal cartel sanctions **only apply to individuals** (and not undertakings) then Reg 1 does **not apply** to its enforcement

✦ Result: only impose criminal sanctions on individuals

✦ **Interpretation 2 (Wils and the Commission):**

✦ Recital 8 does no more than reiterate what is in Article 3(3)

✦ Essentially – Reg 1 will not apply if the criminal offence pursues a **predominant objective** that is not that of **EU competition law**

✦ Result:

(i) create a criminal cartel law that has a different predominant objective (eg punishment of immoral behaviour) OR

(ii) do not prosecute cartels with effect on trade (like Ireland)



(c) Protecting the **administrative leniency** programme

✦ Common ground:

- ✦ Cartels are inherently **secret**
- ✦ (Administrative) immunity/leniency is an **essential element** of effective cartel enforcement
- ✦ We **do not** want criminal sanctions to **undermine** the national leniency programme

✦ Problem:

- ✦ The mere existence of criminal cartel sanctions can (without more) lead to **tensions** with administrative leniency
- ✦ Reasons:
 - ✦ (i) The firm thinking of applying for leniency may care about its employees
 - ✦ (ii) The firm that would like to apply for leniency would like its (past/current) employees to cooperate with it

(c) Protecting the **administrative leniency** programme

✦ Solutions:

✦ (i) Create a **criminal immunity** programme

- ✦ General idea: *automatic* granting of immunity from criminal prosecution to first to report the cartel

- ✦ Possibly with discretion to give immunity to second through the door if it adds significant value to case

- ✦ This helps to protect the reporting individual (and can create additional races to the regulator: Australia)

- ✦ Issue: principle of mandatory prosecution (but can be overcome)

✦ (ii) **Link** the administrative immunity programme with the criminal one

- ✦ Allow for automatic criminal immunity for the (cooperating) employees of the undertaking that has been granted administrative immunity

- ✦ Link should not be complete (Greek experience)

- ✦ Policies should also stand apart to encourage additional races

- ✦ (1) **Criminal** cartel sanctions **should be introduced** in Finland
 - ✦ A solid, albeit imperfect **case for** criminal cartel sanctions exists
 - ✦ Finland currently only employs administrative cartel sanctions and is likely to impose **sub-optimal fines**
 - ✦ Fines should not be increased to their optimal level (due to negative consequences) but criminal sanctions (as a non-indemnifiable sanction) can **fill the ‘deterrence gap’**
 - ✦ Finland is likely to have the ‘competition culture’ needed to support criminal sanctions

- ✦ (2) **Care needs to be taken** in the definition of the offence
 - ✦ The ‘carve out’ of **agreements made openly** (notified to the FCCA or published publicly) should also occur [operationalises Article 101(3) TFEU-type ‘defence’]
 - ✦ The criminal cartel offence should only be applicable to **individuals** and not undertakings [reduces problem with Reg 1/2003]

Part IV: Specific Recommendations



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✦ (3) The Finnish authorities would be advised to ensure that the cartel offence **captures significant moral wrongfulness**

✦ One way of doing this is to **link the offence** to the moral norm against stealing, deception or cheating

Norm	Action Required
Stealing	<ul style="list-style-type: none">- Articulation that consumer welfare (not total welfare) is the relevant standard- Only implemented cartels would be subject to the offence
Deception	<ul style="list-style-type: none">- The 'carve out' of agreements made openly- Only implemented cartels would be subject to the offence
Cheating	<ul style="list-style-type: none">- Requirement of intention to engage in cartel activity would strengthen link with cheating

✦ Also requires Finnish citizens to value the **free market** (to ensure cartels result in agreed 'social harmfulness')



- ✦ (4) Certain **practical measures** should be adopted:
 - ✦ To protect the administrative immunity/leniency regime:
 - (a) A **criminal immunity programme** should be introduced
 - (b) There should be a **link** between administrative immunity and criminal immunity: employees of the immune firm get automatic criminal immunity
 - ✦ A **prioritisation strategy** should be created that ensures support from all stakeholders (particularly consumers)
- ✦ (5) The authorities should *consider* **methods of reducing the costs** of criminalisation:
 - ✦ Plea-bargaining (like the US) [admittedly controversial and not without its own problems]
 - ✦ ** Imposition of **cost orders** on convicted cartelists (like Ireland)



Questions?

p.whelan@leeds.ac.uk

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The Criminalization
of European Cartel
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Theoretical, Legal, and
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Peter Whelan

