GROUP LITIGATION IN EUROPEAN COMPETITION LAW

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A Law and Economics Perspective

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FOREWORD

Prof. Roberto Pardolesi*

There are two basic approaches to deterring socially harmful behaviour: enforcement by public agencies and litigation by private parties. Most countries use both approaches, though to varying degrees. The United States of America characteristically relies on private enforcement across the board: these litigation options are less relied upon in the European Union (EU), where public enforcement tends to be the favoured lever.

Common sense suggests, by and large, that private enforcement, if effectively designed, will lead to an increased probability of detecting illegal conduct and accuracy of fact-finding. This, in turn, would increase the workload of the courts and trial costs for private parties.

However, in the antitrust field there may be more arguments for public enforcement than in other areas. On the one hand, public enforcement is commonly deemed superior in pursuing the objectives of deterrence (more investigative powers, more effective sanctions, better control of their measure, more reliable commitment), and in clarifying the content of the antitrust prohibitions. On the other hand, even if better suited to pursue corrective justice, private enforcement might work poorly. Reasons for this include: if victims of antitrust law infringements are private consumers, harm and causation are typically not obvious to the victims; the detection of infringements requires investigation by experts, and public authorities are often better prepared (and informed: but this is a contentious issue) than the victims; and, since the total harm caused by infringements of competition law is often spread across many victims, even well-informed victims have little incentive to bring damages claims.

The final stroke against private enforcement is even more devastating: facilitating access to civil courts in antitrust cases increases the risk that private damage actions will be abused by competitors. In fact, plaintiffs are often competitors or takeover targets of defendants. They may have an incentive to employ private enforcement strategically, in order to: 1) prevent large potential competitors from

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entering their market or competing vigorously; 2) extort funds from successful rivals; 3) improve contractual conditions; 4) enforce tacit collusive agreements; and, 5) respond to existing suits, or hostile takeovers. The extent to which firms strategically abuse the antitrust laws under private enforcement depends crucially on the structure of damage awards in private antitrust cases. Where available, punitive damages (and the variation on the same theme, represented by disgorgement of profits) reduce firms' incentives to violate antitrust laws, but also increase their incentives to use antitrust laws strategically against their rivals. The actions that are taken to extort money are often resolved through the payment of a "tax on success" for the firms whose positions are sought after by competitors. However, taxes on success discourage investment and innovation, which harms consumers.

Moreover, it has been recently claimed that in the EU the accumulation of sanctions (which over time have been consistently aggravated) and damages might have an over-deterrent effect. Suppose, for the sake of clarifying this non-obvious argument, that a firm with an annual turnover of € 100 million joins a cartel (which is expected to last 7 years) and imposes an overcharge of, say, 15%. Apply a reasonable discount rate of 8%. The total expected profit from the participation to the cartel will be ca. € 84 million. Taking note that, in Europe, the average fine for a cartel member climbed in 2007 to € 75 million, one should consider that the firm risks paying a € 10 million fine (10% of the yearly total turnover, which might be referred to a host of products, beside the cartelized one), plus damages for € 84 million, plus legal costs of 10 to 20% of the awarded damages, plus reputational loss, plus wasted managerial resources in handling litigation: a total bill of over € 120 million. Carrying out such a computation forces the conclusion that too much is simply too much.

To further darken the picture, critics have pointed out that, where private enforcement is widespread, private actions too often result in remedies that provide lucrative attorney's fees but secure no real benefits for overcharged purchasers, are parasitic and "dramatically overreaching" (Kovacic).

Yet, as remarked by other commentators, administrative fines will often be insufficient to achieve the optimal level of deterrence. Diffuse recidivism strongly supports the idea that cartelizing is a promising activity. Looking at the 18 cartels which were the subject of decisions during the years 2005 to 2007, and assuming an overcharge of between 5% to 15%, the European Commission (2009) has estimated a total harm ranging from around € 4 billion to € 11 billion. Taking the middle point of this overcharge range – 10% – provides a conservative estimate of consumer harm of € 7.6 billion due to these cartels. This harm should be compared to the total amount of fines, which is € 5.9 billion. This comparison

hints at the conclusion that cartelizing is still convenient, especially if one considers cartels which are not discovered.

Accordingly, there seem to be considerable advantages to having a system in place for private actions. First, private enforcement of competition laws can be a formidable deterrent to such conduct. Second, they help to ensure that the victims of unlawful conduct are compensated. Third, allowing private actions relieves some of the enforcement burden from public competition agencies, which do not always have sufficient funding to pursue every matter that is worth pursuing.

This being the case, private claims for damages caused by antitrust violations should provide, to say the least, a complement to public enforcement. Actually, this is the view recently adopted by the European Commission. In its view, compensation of antitrust damages is to be regarded as fundamental. Victims (all victims of all breaches of Article 101 and 102 TFEU in all sectors of the economy) should get full restoration of the prejudice suffered; and law-abiding businesses should not suffer from a competitive disadvantage. An increased level of actions for damages will also have the effect of increasing deterrence for potential infringers. Purporting to implement a "genuinely European system", the Commission emphasizes its commitment to preserve an effective public enforcement. The crucial role of the public authorities remains the main pillar; however, it should be complemented by a second pillar, private damages actions, never mind whether relying, or not, on a prior finding of an infringement by a competition authority (and thus both follow-on and stand-alone suits).

In this work, Sonja Keske explores the 'philosophic' foundations of this approach. The scenario is extremely complicated. Some issues – such as fault requirement, fee shifting and, to a lesser degree, the standing of indirect purchasers (but cf. the German experience) appear relatively undisputed. Other issues still raise bitter discussions.

Among them, a pivotal role is to be ascribed to collective redress. Whereas the necessity to provide for means of collective redress amenable to all categories of victims of competition law infringements goes without saying, the means to achieve this goal are hotly debated, not only in the antitrust framework, above all because of concerns about misuse of the system.

Keske's work focuses precisely on the uneasy fate of group litigation in the antitrust field. The problem is multi-faceted, and exposed to the risk of unmanageability. Abiding by the scientific imperative of reducing complexity, and deploying the armoury of law and economics, she privileges the perspective of deterrence. As the author candidly recognizes, such one-dimensional analysis

largely neglects other relevant aspects. But the insights it provides are significant, and extremely challenging. A telling example: the shyness of the Commission in preferring an opt-in system, because of the avowed evils of the American class-action style, is to be scrutinized through the paradigm of mandatory procedures, where all the members of the concerned group are automatically represented in the collective suit. No surprise, then, that the analysis evolves toward unexplored frontiers, like auction mechanisms in determining the agent responsible for the final relief.

Harsh as it may appear in its uncompromising trajectory, Keske's work is a precious start of a still long journey.

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LIST OF ABBREVIATIONS

Art.	Article
ATE (insurance)	After-the-event (insurance)
BB	Betriebs-Berater
BGB	Bürgerliches Gesetzbuch (Civil Law Code)
BGH	Bundesgerichtshof (Federal Court of Justice)
BGHZ	Collection of decisions by the BGH
BörsG	Börsengesetz (Stock Exchange Act)
BRAO	Bundesrechtsanwaltsordnung (Federal Lawyer's Act)
BVerfG	Bundesverfassungsgericht (Federal Constitutional Court)
CA	Competition Act
CAFA	Class Action Fairness Act
CAT	Competition Appeal Tribunal
CAT R	Competition Appeal Tribunal Rules
CDC	Cartel Damage Claims company
CFI	European Court of First Instance (now: General Court)
CFAO	Conditional Fee Arrangements Orders
CFAR	Conditional Fee Arrangements Regulations
Commission	European Commission (Commission of the European Communities)
Community	Community of the European Union
CPR	Rules on Civil Procedure
e.g.	exempli gratiā (for example)
EC	European Community
ECJ	European Court of Justice (now: Court of Justice of the European Union)
EC Treaty	Consolidated version of The Treaty Establishing the European Community
Ed.	Editor
et al.	et alii / et aliae (and others)
EU	European Union
European Commission	Commission of the European Communities
FCA	Federal Competition Authority (Bundeskartellamt)
FRCP	Federal Rules of Civil Procedure (US)

GLO	Group Litigation Order
GWB	Gesetz gegen Wettbewerbsbeschränkungen (Competition Law)
GRUR	Gewerblicher Rechtsschutz und Urheberrecht
i.e.	id est (that is)
KapMuG	Gesetz über Musterverfahren in kapitalmarktrechtlichen Streitigkeiten (Capital Market Test Case Act)
LEC	Ley de Enjuiciamiento Civil
LEI	Legal Expense Insurance
LG	Landgericht (Regional Court)
LSC	Legal Services Commission
Member States	Member States of the European Union
NJW	Neue Juristische Wochenzeitschrift
OECD	Organisation for Economic Co-operation and Development
OJ	Official Journal of the European Union
P.E.	Private Enforcer
PD	Practice Direction
OLG	Oberlandesgericht (Higher Regional Court)
R&D	Research and Development
RVG	Rechtsanwaltsvergütungsgesetzes (Law on remuneration of lawyers)
TEU	Consolidated Version of the Treaty on the European Union
TFEU	Consolidated Version of The Treaty on the Functioning of the European Union
Treaty of Lisbon	Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community
UK	United Kingdom
UrhG	Gesetz über Urheberrecht und verwandte Schutzrechte (Law on Copy Rights and Related Rights)
US	United States of America
USA	United States of America
U.S.C.	United States Code
UWG	Gesetz gegen den unlauteren Wettbewerb (Law Against Unfair Competition)
VBER	Vertical Block Exemption Regulation
ZPO	Zivilprozessordnung (Rules on Civil Procedure)

PREFACE

The economic losses caused to society by competition law infringements are significant. A few exemplary estimates may assist in clarifying the amounts at stake. For example, in the United Kindom (UK), annual losses due to monopolistic behaviour are estimated to be between £ 4.5 billion and £ 9 billion.[1] Enforcement of competition law is perceived as being able to reduce these losses. In the United States of America (USA), the yearly benefit, or avoided losses, achieved by the albeit not perfect enforcement system is estimated at US$ 50 to US$ 100 billion per year.[2] For Australia, the OECD estimates the yearly benefit of their effective competition policy at 2.5 percent of gross domestic product (GDP).[3] In Europe, 2.5 percent of GPD would amount to around € 396 billion per year. Whatever the exact figures may be, it is safe to say that such figures are anything but "peanuts." Therefore it is crucial that efficient enforcement systems are developed that sufficiently deter harmful anticompetitive practices and minimise the corresponding social welfare losses.

Due to the potential for such enormous losses, several avenues by which to achieve efficient enforcement of competition rules are currently being pursued by European legislators. First, there has been a tendency towards strengthening the investigative powers of competition authorities.[4] Second, like the UK and Ireland, other Member States are discussing the possibility of using criminalisation of competition law infringements as a tool to achieve more efficient and effective deterrence against anticompetitive behaviour.[5] A third avenue, which is being strongly pursued not only by the European Commission,

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1 Organization for Economic Co-operation and Development, "Report on the Nature and Impact of Hard Core Cartels and Sanctions against Cartels under National Competition Laws," (2002) 7, 2.Organization for Economic Co-operation and Development, "The Role of Competition Policy in Regulatory Reform, OECD Reviews of Regulatory Reform, Reform of the United Kingdom " (2002) 55. Available at: www.oecd.org/dataoecd/2/61/27068497.pdf.

2 See Baker, "The case for antitrust enforcement," *Journal of Economic Perspectives* 17 (2003): 27.

3 Renda, et al, "Making antitrust damages actions in the EU more effective. Study in support of the impact assessment of the EC White Paper on antitrust damages actions," (2007) 92.

4 Wils, "Is criminalization of EU competition law the answer?" *World Competition: Law and Economics Review* 28 (2005): 117, 136.

5 See for example the contributions by Luna and DeLong, discussing the risks and costs connected to an overextension of criminal law. Luna, *Overextending the Criminal Law. Go Directly to Jail: The Criminalization of Almost Everything.* ed. Healy. Washington DC: Cato Institute (2004), 1; DeLong, *The New 'Criminal' Classes: Legal Sanctions and Business*

is to increase competition law enforcement and its deterrence effect by strengthening private enforcement. It is in pursuing this last avenue where the introduction of a group litigation mechanism plays a vital role. As a consequence, increased information regarding the most efficient way to design a group litigation mechanism, the benefits and costs incurred by choosing one specific variation over other alternatives, and what other legal rules and principles will affect the overall performance, are paramount. Some answers to these questions are presented in this book.

The goal of group litigation, as it is discussed in Europe, is to utilise the long grown and well-established basics of tort regulation as they exist in the various Member States to foster private enforcement. Other avenues may also be taken to enforce competition law. For example, Competition Authorities could be endowed with more resources and power. Alternatively, public enforcement could be improved by instigating solutions to perceived inefficiencies of public enforcement. Criminal law could be made applicable. Also, additional public bodies could be created and charged with the task of investigating markets and firms to detect competition law infringements. However all these avenues are beyond the realm of this book. The concern here is with the question of, if and how private actions for damages may assist to protect competition and thereby ultimately benefit the consumer. To be more precise, the focus is on the potential role group litigation mechanisms in actions for damages could play. In order to concentrate on this question, it is of course necessary to omit detailed investigations of other important and currently discussed issues, such as the still ongoing debate of private versus public enforcement. Moreover, other debated features of private actions for damages, inter alia: the correct way to calculate damages, whether or not to allow for a passing-on defence, or all the different possibilities to finance such litigations, are not dealt with in depth in this analysis. There are many other excellent pieces of work, which I refer to when applicable, which do deal with these matters.

Current developments on the European level, as well as in individual Member States suggest that soon there will be some form of private enforcement with group litigation in actions for damages due to competition law infringements in most if not all Member States. This is the starting point of this analysis. The use of class actions in antitrust law is a well known and established concept in the USA and other common law countries, such as Canada or Australia. However, group litigation in general and especially in competition law cases has not been widely used in the European Union Member Staes. Therefore, empirical research into the (in-)effectiveness of group litigation in the case of infringement of

Managers. Go Directly to Jail: The Criminalization of Almost Everything. ed. Healy. Washington DC: Cato Institute (2004), 9.

European competition law remains a point of research for the future, once different systems are introduced and allowed to operate sufficiently long in the various Member States.

The analytical approach used in conducting the theoretical analysis throughout this book involves a Law and Economics approach. This approach is founded on various streams of legal and economic literature concerned with, not only competition policy, but also the theory of crime and punishment, as well as litigation theory. These streams are then combinined to develop an integrated and consistent framework. As a consequence, the analysis in this book focuses on the goal of deterrence, rather than that of compensation, and also on stand-alone actions rather than follow-on actions.[6] The efficiency of substantive rules of competition law or their public enforcement is not evaluated. Rather, the analysis rests on the assumption that the imposition of the optimal fine, as developed in deterrence theory, will lead to total welfare increase by increasing compliance with competition laws and only allowing total welfare enhancing breaches. Another assumption made is that public enforcement as it exists is not perfect and does not detect and/or deter all infringements, so that private enforcement may increase deterrence as a second enforcement pillar. Further research may provide more detailed insights into the costs and benefits of such enforcement of competition law activities and allow a more accurate evaluation of the effects on total welfare. It may also allow a cost-benefit comparison of private versus public enforcement. Moreover, just as in the case of competition law, the firm will be treated as one entity, not taking in account considerations that are dealt with in the stream of corporate governance literature and others. The harmonisation costs or costs of legal change are also not taken into account. These can differ greatly from one legal system to another and would have to be weighed against any increase in total welfare the specific group litigation systems may bring about.

Despite these limitations of the analysis conducted here, many of the obstacles to efficient group litigations discussed under the chosen approach are also relevant for follow-on actions as well as for other areas of law than competition law. Moreover, the insights developed here within the context of pursuing the goal of deterrence will also be highly relevant to any analysis or evaluation where compensatory justice is set as the overriding goal. In that case, the trade-offs between the features that make a particular litigation mechanism efficient or effective and compensatory justice are most relevant. While not the focus of this analysis, at least the former, but sometimes also the latter side of these trade-offs are identified in this work. Moreover, these issues are also discussed in the

6 A focus on stand-alone actions is a consequence of focusing on the goal of deterrence, as will be shown in Chapter 3.

analysis of the legal changes proposed by the European Commission and in the legal comparison of the regimes implemented in the USA, UK and Germany. The analysis therefore is also able to provide insights for other approaches.

The book is structured as follows. Chapter 1 provides an overview of the placement of the topic in the context of the general debate about enforcement of competition law and the recent developments concerning private enforcement of competition law in the European Union. In chapter 2, the general framework used throughout this book is established. Relevant terms and concepts are defined and the general legal and economic framework established. Chapter 3 applies the framework established in the previous chapter to analyse generalised forms of existing forms of group litigation mechanisms, i.e. collective actions and representative actions. The insights gained in this analysis are then used to develop a form of group litigation, which is designed to be more efficient than previous forms, i.e. a market based mechanism combined with auctions. In chapter 4, the proposals made by the European Commission in the Green Paper and the ensuing White Paper are measured against this benchmark as developed in chapter 3, to provide an analysis as to whether they will generate efficient deterrence. As deterrence is not the primary goal for the Commission's position, also other goals as defined by the European Commission and potential legal obstacles are described and discussed with regard to the results developed in chapter 3. Chapter 5 provides a legal comparison of group litigation mechansims found in three selected legal systems: the USA, UK and Germany. The book concludes in chapter 6 by reaching some overall conclusions and policy implications of the results.[7]

[7] Legislative and policy developments as well as case law could only be taken into account until August 2009. Advances after that have not been incorporated, except for the notation changes brought about by the Lisbon Treaty coming into effect December 2009.