

Barbarians At The Gate?

By Dr. Kees Jan Kuilwijk and Kenneth P. Ewing

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Wednesday, May 02, 2007 --- Say "treble damages" and "class actions" in one sentence to a European Union competition lawyer and you are likely to receive an earful about "importing" the worst of the U.S. antitrust enforcement regime into Europe. Add "lawyers' fees" and the volume of the response will go up. Yet increasing the attractiveness and effectiveness of private civil enforcement of EU competition law tops the competition policy agenda for the European Commission. Are the barbarians banging on the EU gates? Is the Commission inviting them in?

First some background. From the very inception of the European Communities, it has been clear that the competition rules (now in Articles 81 and 82 of the European Union Treaty) can be enforced by private parties as well as the Commission and national governments. Indeed, private enforcement—the application of EU competition law in civil disputes before national courts—has historically played a role clarifying the scope of competition law in Europe.

In 2001, the European Court of Justice also made clear that national governments may not inhibit such private civil enforcement, but there is no EU-wide system or set of rules about how injured private parties may proceed to secure recompense. To the contrary, potential private plaintiffs must look to their—by now 27—national legal regimes for specific causes of action, the procedural requirements, and the quantum of damages and other remedies available to them. Perhaps as no surprise, civil damages for breaches of EU competition law have been rare, particularly in the most egregious cases, namely large-scale cartels involving price fixing.

Soon after her appointment in the fall of 2004, EU Commissioner for Competition Neelie Kroes led the charge to fill this gap between public and private enforcement in the EU. In 2005 the Commission staff prepared a working paper and a Green Paper identifying the reasons for the paucity of private enforcement in the EU and tentatively outlining possible solutions.

Commissioner Kroes also took to the lecture circuit, speaking forcefully in favor of Europe-wide action to encourage civil damages suits by victims of antitrust violations. A three-day conference on the subject was held in March of this year, and on April 27 the European Parliament expressed its approval of the general concept. A formal White Paper with concrete legislative recommendations is expected by the end of 2007.

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Barbarians At The Gate?

What is being considered? At this point no concrete proposals have been made, but the Green Paper asked for comment on several possible measures including mandating the amounts of damages and interest that should be paid for violations—double damages in the case of horizontal cartels; a uniform rule that fault be presumed if the Commission proves a violation; some method of aggregating consumer claims; and requiring defendants to disclose documents to plaintiffs.

Other issues to address, albeit with no tentative proposals yet, were how to handle indirect purchasers; how to reduce the cost of bringing damages claims; and coordinating private with public enforcement, particularly to avoid undermining the Commission's successful leniency program that uncovers many of the worst cartels.

The Commission's stated goals in all this are clear: to enhance deterrence of antitrust violations and to increase compensation of victims. The theory is that liability for civil damages in addition to public fines will deter more potential cartelists than fines alone. Because not every cartel is discovered and bringing suit costs a lot of money, however, something more than compensation for actual damages is needed.

Treble damages, class actions, and compensation of private plaintiffs' lawyers if they win (often under "contingent fee" agreements that require no payment if they lose) is how the United States has historically sought to achieve the same goals.

Thus in the U.S., governmental enforcement against price fixers routinely spawns a feeding frenzy of private treble damage complaints, usually by plaintiffs seeking to represent an entire class of similarly situated purchasers, brought by specialist lawyers seeking fees guaranteed by statute if they win. Very often absent class members would likely never sue on their own but have a chance for some monetary compensation thanks to the efficiency of the class action mechanism and the attractions of treble damages and free legal services. As a consequence, although cartel fines often seem higher in the EU than in the U.S., total payments for participating in a major price fixing cartel usually end up much higher in the U.S., when the private "follow-on" damages claims are taken into account.

But it is precisely these three aspects of the U.S. model that evoke the strongest negative reactions in Europe, and not without some justification. Take treble damages first. On the one hand, it has been argued, by McAfee and others, that the prospect of a verdict of treble damages against a competitor furthers the "strategic abuse of antitrust laws." On the other hand, economic studies of how public sanctions work show that fines must be multiplied by a factor that is

Barbarians At The Gate?

inversely proportional to the probability that the offender will be caught and convicted.

Empirical research in the United States by Bryant and Eckhard has shown that probability rates for discovery of price fixing arrangements are slim, not higher than 17% at the most. By that measure, effective deterrence would require total costs (fines plus civil damages plus costs of defense) to equal—not two or three—but six times the gain expected from the violation.

One might be tempted to impose such a high multiplier to achieve the economically sound level of deterrence, but at some point one must also recognize that it is current and future customers who will ultimately pay these damages through higher product prices. That is precisely what happened after the famed Tobacco Settlement ended the extremely complex civil damages suits in the U.S. against tobacco companies in the 1990s and cigarette smokers immediately saw the price jump to 45 cents per pack, the precise amount needed to pay the agreed damages over time.

The class action procedural mechanism raises similarly serious issues. The main benefit is also the main problem. For the class member not likely to sue on her own is also not likely to pay much attention to the lawsuit brought on her behalf—even if she knows about it! And by joining many such "absent plaintiffs' claims, the mechanism increases the lawyer's obligations to those new clients while perversely reducing the influence of the original named plaintiffs. In short, the lawyer comes to control the litigation and may not always follow the best interests of the class members.

Outcome-related fee awards exacerbate this classic "principal-agent" problem. If the lawyer is truly paid only if he wins, as in the U.S. "contingent fee" arrangement, then plaintiffs have literally nothing to lose from bringing suit. But the lawyer fronting the costs of uncovering evidence and preparing the case sees only rising costs and an incentive to settle the case as soon as an acceptable return on that "investment" can be secured by agreement with the defendants.

It is for this reason that in the U.S. courts must approve both settlements and attorneys' fees, but an early settlement, before a full airing of evidence at trial, can make it hard for any judge to assess the actual benefits for the class members. So-called "coupon settlements"—in which class members receive little or no cash compensation but instead receive coupons or discounts off further purchases from defendants—are a much-derided example of how even court-approved settlements seem not to benefit victims as much as plaintiffs' lawyers and perhaps even defendants themselves.

Barbarians At The Gate?

In the end, it appears that the Commission seeks to steer a middle course hoping to avoid the worst excesses of the United States' "litigation culture" while also enhancing the effectiveness of European competition law. It is too early to say precisely what will come out of this process, but the debate has itself increased the visibility of existing mechanisms for civil damages recovery, and we may soon see the tiny trickle of such cases under present laws increase to a small stream. Indeed, if the increased international collaboration among experienced antitrust plaintiffs' lawyers and the increasing inclusion of non-U.S. plaintiffs in U.S. antitrust suits is any indication, that small stream may grow fairly quickly.

In other words, whether invited or not, they are already inside the gates.

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