Market and Competition Law Review / VOLUME VI / No. 2 / OCTOBER 2022

The Impact of the Damages Directive on the Enforcement of EU Competition Law

Philipp Kirst

*Reviewed by Catarina Vieira Peres de Fraipont**

The question of how to combine public and private enforcement to achieve optimal results in terms of effective enforcement and deterrence of anti-competitive behaviour is a trending one in national and EU enforcers' minds. Recently, the head of the *Bundeskartellamt*, Andreas Mundt, admitted to being worried about the decline in leniency applications as undertakings fear follow-on damage claims. The worry is comprehensible given that about half of Germany's cartel cases are triggered by leniency applications. Tackling the decline in leniency applications due to fears of follow-on damage claims has become a key priority of the *Bundeskartellamt*.[1]

The same worry plagues the European Commission, which is also investigating how the increase in private compensation claims is decreasing the attractiveness of applying for leniency, and whether it should adapt to the new reality. Margareth Vestager has publicly recognized that "risks are increasing" for companies applying for immunity as a result of the growing popularity of damage claims, which could "shift the balance of risks" for companies and decrease the attractiveness of the leniency programme.[2]

In this scenario, Philipp Kirst's *The Impact of the Damages Directive on the Enforcement of EU Competition Law* is a timely and necessary book for competition authorities and legislators in search of guidance. Through a thorough legal and economic analysis, the author addresses the question

DOI: https://doi.org/10.34632/mclawreview.2022.11718

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[1] Francesca Micheletti, "BKartA head says immunity from follow-on actions for leniency applicants remains on the agenda – Georgetown 2021" PaRR (parr-global.com), 14 September 2021.

[2] Speech by Margareth Vestager at the Italian Antitrust Association Annual Conference – "A new era of cartel enforcement", 22 October 2021.

of how public and private enforcement can be best combined to effectively enforce EU competition rules.

The book focuses on three aspects the author deems crucial to achieve optimal balance between private and public enforcement, namely (*i*) the allocation of civil liability among infringers, (*ii*) the EU leniency programme, and (*iii*) the method for setting fines. The author then proceeds to making concrete legislative proposals to overcome the negative effects that may arise from the increasing attractiveness of damages claims.

In the introductory part, Kirst describes the EU enforcement system and the Damages Directive. The author points out that, despite the vast literature on the benefits of a mixed enforcement system, it is a tough endeavour to find the right balance between public and private enforcement instruments, one which does not jeopardize the effectiveness of the tools used and achieves optimal levels of deterrence.

Part I of the book describes the legislative process that led to the entry into force of the Damages Directive and outlines its provisions. The author demonstrates that, despite the Directive's objective of creating a level playing field in Europe, substantial divergences among Member States remain.

The allocation of civil liability among infringers in light of the Damages Directive

The allocation of civil liability among infringers is discussed in Part II of the book.

Under article 11, no. 5 of the Directive, Member States must ensure that infringers may recover a contribution from other infringers, the amount of which should be determined *in the light of their relative responsibility for the harm caused* and, in case of immunity recipients, cannot exceed the amount of harm caused to the latter's direct and indirect purchasers.

The author begins by describing the debate in the US, where a no-contribution rule prevails, and concludes that its advantages (increase in deterrence, in settlement agreements and in administrative efficiencies) are outweighed by its significant negative implications (lack of fairness and corrective justice concerns) and, therefore, the Directive's choice of adopting a contribution rule should be welcome.

According to recital 37 of the Directive, the determination of the share of relative responsibility of a given infringer and the relevant criteria, such as turnover, market share, or role in the cartel, is a matter for the applicable national law. The author examines all the possible criteria for

the determination of relative responsibility and concludes that none is, in itself, sufficient. The author thus recommends a case-specific application of a combination of different allocation rules. In particular, the author suggests using a combination of two rules: (1) a gain-based allocation for *direct and indirect purchasers*, and (2) an allocation based on market shares for *other claimants*. According to the author, these allocation rules score better than any other individual rule under corrective justice or deterrence considerations and optimally balance the goal of accurate determination of individual responsibility with administrative efficiency.

However, since these allocation rules do not take into account the infringer's role in the infringement, the author sets out to find a method suitable for quantifying it. To that effect, Kirst suggests aligning the attribution of civil liability with the Commission's practice of adjusting the basic amount of the fine under the Fines Guidelines.[3] The author analyses the Commission's fining practice with the aim of determining which factors related to the role played in the cartel were accepted as mitigating or aggravating circumstances, and whether a methodology for the quantification of the adjustments could be derived from the Commission's practice, which could then be applied to adjust the distribution of civil liability between co-infringers. Even though no coherent methodology on the reduction of mitigating factors could be deduced from the reviewed period (2001-2020), regarding aggravating circumstances for infringement leaders and instigators, the Commission consistently applies an increase of 30% or 50%, depending on whether one or two such circumstances are present. The author argues that an increase of civil liability for the instigator or leader could also have positive effects on settlements and, if the settlement is made dependent on the plaintiff's disclosure of further information, this could, in turn, accelerate the claimant's litigation against other members of the cartel.

The impact of the Damages Directive on the EU Leniency Programme

The optimization between public and private enforcement is a difficult balancing act since, on the one hand, from a compensatory justice perspective, victims of cartel infringements should be compensated (redressed?) for the

[3] Guidelines on the method of setting fines imposed pursuant to Article 23 (2) (a) of Regulation No. 1/2003, C210/2 [2006] (2006 Fines Guidelines).

entire harm suffered, but, on the other, the number of leniency applications will decline if immunity recipients are not protected from damage claims. In such case, the benefits achieved through better compensation may be outweighed by the reduction in the detection of infringements, and the balance between private and public enforcement will be suboptimal.

The Directive tries to achieve an adequate balance by denying private parties access to leniency statements (article 6). Moreover, immunity recipients are not obliged to compensate all injured parties but only their direct and indirect purchasers (article 11), unless injured parties fail to obtain full compensation from other undertakings (article 11 no. 3). Furthermore, a rebuttable presumption that the cartel caused harm was introduced (article 17 no. 2), and judges are empowered to estimate the harm suffered (article 17 no. 1).

In the third part of the book, Kirst discusses the trade-offs between the right to compensation and an effective leniency programme from a law and economics perspective.

The discussion begins with a description of EU and Member States' case law and legislation on leniency programmes and access to documents that existed prior to the entry into force of the Directive. The main provisions of the Directive regarding compensation, the binding effect of national competition authority's decisions, presumption of harm, disclosure of evidence, joint and several liability, and the liability cap for immunity recipients are then summarized.

With the help of insights from game theory, Kirst considers the impact of the Directive on the effectiveness of the leniency programme. In particular, the author analyses how the Directive may negatively affect the incentives of cartel members to confess, and searches for an alternative solution capable of providing a better trade-off between compensation and optimal leniency incentives.

The author demonstrates that, with the Directive's regime in place, the overall risk of disclosure of evidence and the cost of cooperation increases significantly under the leniency programme (even though the likelihood of disclosure might be higher in some Member States than others). This reduction in leniency incentives is problematic, because the benefits achieved through better compensation will be outweighed by the reduced discovery of cartels.

As such, the author suggests an alternative solution, which, by providing more leniency incentives, is likely to lead to a better interaction between

public and private enforcement. Kirst argues that, under certain conditions, the goals of deterrence and justice could be better achieved by granting immunity or reducing damages in the same proportion as fines are waived or reduced under the leniency programme. In other words, cartel participants granted immunity or benefitting from a reduction in fines would receive the same protection from damages liability. The author suggests shifting the obligation to pay damages from the immunity recipient to the cartel participants who did not cooperate with the competition authorities. Yet, Kirst draws an exception, namely whenever full compensation of injured parties is not possible.

Reconciling fines and damages

In the fourth part of the book, Kirst rightly points out that, if the Directive succeeds in fostering private enforcement in Europe, the existent fining methodology will probably lead to a situation of over-deterrence, thereby reducing welfare enhancing transactions.

As the European Court of Justice has repeatedly affirmed, the objective of antitrust sanctions, and the Commission's guiding principle for the calculation of fines, is deterrence. However, according to recent literature summarized by Kirst, the current method of calculating fines (based on the sales value of the previous year) is incomprehensible and incapable of leading to an optimal level of deterrence.

The author, thus, proposes a new method for calculating fines based on the infringer's gains. This alternative approach has a twofold objective. First, it seeks to avoid overdeterrence without jeopardizing compensation of injured parties. Second, it strives to ensure that the costs of infringing antitrust norms will always exceed illicit gains, thereby preventing future infringements.

According to the proposed methodology, the calculation of fines incorporates the anticipated civil liability into the determination of the basic amount. Instead of deriving fines from sales revenues of previous years, the fine is calculated on the basis of the overcharge of the cartel and is then adjusted by either aggravating or mitigating factors. The competition authority would impose a security of the estimated damages, which would only be reimbursed after the infringer has compensated all the claims (as part of a settlement or a judicial decision).

Kirst recognizes, however, that the inclusion of damages in the calculation of fines may encounter several obstacles.

The first hurdle identified by the author relates to the fact that cartels are likely to have different welfare standards, as different groups of victims may have suffered a loss. The author argues that, given the difficulty in estimating the harm caused to all potential claimants, the estimation of civil liability should be limited to the price effect for direct purchasers, based on the calculation of over-charge (thus excluding the possibility of a passing-on defence). Kirst draws, however, an exception regarding cases where competition authorities are aware and able to calculate damages suffered by victims other than direct or indirect purchasers.

The second obstacle of the proposed methodology relates to the fact that damages need to be calculated before they are claimed. This is problematic given that the number of damages known to an authority at the time of the infringement decision is often very different from the final amount awarded by courts. The author argues that authorities should overcome such hurdle by estimating damages from an *ex-ante* perspective.

The third issue relates to the standard of proof to be applied for the harm caused. Investigating the damage caused by an infringement is obviously a very lengthy and resource-intensive process. The risk of being unable to find evidence for the estimation of the overcharge lies with the competition authority. Moreover, not every cartel necessarily leads to a loss for the purchasers of the goods or services subject to the infringement. As such, if the burden of proof is not eased for the authorities, fines will likely be set at a level lower than optimal. Thus, the author argues that, in cases where the calculation is disproportionately difficult, competition authorities should be able to rely on presumptions of overcharges, thus preserving part of their resources for law enforcement. However, overcharge estimates should be applied with caution. Empirical studies have mixed results and point to a very broad range of overcharges (from 49 per cent to 15.5 per cent). Therefore, it is the author's belief that presumptions of harm applied by competition authorities for the calculation of fines should not have a binding effect before civil courts.

Another question that the suggested methodology for the calculation of fines raises relates to the appropriate standard of proof for the causal relationship between the harm and the infringement. Given that neither the identity of claimants nor their individual harm is known at the time when the authority estimates civil liability to set the amount of a fine, the author argues that the only suitable approach is to apply a general theory of causation, which concentrates on the overall harm caused. This theory

generalizes the harm caused to a group without requiring an individual link between the infringement and the harm.

Furthermore, given that the quantification of harm is highly resource-intensive, the author believes that authorities should cooperate with injured parties to collect information to estimate the harm.

Through economic analysis, the author then illustrates how the proposed methodology ensures that fines are set at an optimal level and identifies all its advantages compared with the current method: (i) the proposed method, by no longer addressing fines and damages in isolation, prevents over-deterrence; (ii) at the same time, under-deterrence is avoided, as it creates certainty for the infringer that the gains from the infringement will be redistributed; (iii) while the method requires intensive price data, the calculation of harm by competition authorities is still administrable; and (iv) even though damages are taken as the basis for the calculation of the fine, the approach guarantees the separation of powers, as courts are not bound by the estimated damages.

Moreover, according to Kirst, the suggested methodology for the calculation of fines respects the principles of proportionality and equal treatment adequately. Whereas, under the current method, as the fine is set regardless of potential damage claims, undertakings with substantially higher civil liability may be penalized significantly harder than others with no objective justification.

Concluding remarks

Kirst concludes by remarking that further research is necessary on how the different standards between Member-States influence the outcome of the proposals of the study. Moreover, the author argues that it is necessary to extend the research question to the global scale to analyse how different regimes influence the results.

The question of how to better align public and private enforcement was addressed by the author only by reference to price-fixing cartels. Thus, further research is needed regarding other types of antitrust infringements, and with different constellations of infringers.

Comment

The problem of over-deterrence in competition law enforcement and the costs which it might entail are rarely addressed by commentators. However, with actions for damages becoming increasingly popular throughout the

EU, this is a pressing issue. Kirst's research is therefore both welcome and necessary.

The book reflects a thorough research, and the author's ideas are well presented and organized. The language is clear. The succinct introduction and conclusion at the beginning and end of each chapter facilitates the reading and consultation of the work. The alternative methods proposed have been exhaustively thought through. The author does not shy away from recognizing potential obstacles, and suggests sensible solutions to overcome them. On the downside, the book could have been more carefully edited, since a number of typos can be easily detected.

All in all, Philipp Kirst's *The Impact of the Damages Directive on the Enforcement of EU Competition Law* is a must addition to the libraries of competition law enforcers, practitioners, and scholars.