EU Cartel Fining Laws and Policies in Urgent Need of Reform

A Rebuttal to Philip Lowe's Article, Cartels, Fines, and Due Process

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I. INTRODUCTION

The criticisms against the cartel fining policies of the European Commission are mounting.² Feeling the heat, the Commission is finally entering the debate: that’s good news. The bad news is that the Commission keeps stonewalling.³ Philip Lowe's GCP online article⁴ is an eloquent case in point. While he deserves credit for publicly addressing some of the major substantive and procedural critiques against the Commission's cartel fining policies, his defensive posture is disappointing and sobering. The head of the Directorate General for Competition (“DG COMP”) pays only scant attention to the concept of due process. Important arguments against the insufficient legal basis under which the current EU cartel fining regime operates are being ignored or sidestepped.

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At least as serious, Lowe’s article overlooks crucial questions relating to the effective prevention of cartel law violations. The perennial agency problem in corporate governance or the fundamental concept of organizational fault are not even taken into account. As a consequence, the recent runaway corporate fines are not being critically tested. It becomes obvious that the current EU cartel law administration is happy with the status quo.  

II. UNDUE "DUE PROCESS"

The cartel fines imposed by the Commission are by now the highest in the World. This in itself calls for very high procedural standards in adjudicating cartel cases. The reality is on the opposite end, however. Even basic checks and balances are lacking. Above all, there is no proper separation of powers. The Commission, a purely political body, acts as both prosecutor and judge. In addition, the legal basis for levying fines, i.e. Sec. 23 of Reg. 1/2003, leaves the Commission with almost unlimited discretion in setting the amounts of fines. Recognizing this, the Commission has itself issued Fining Guidelines, making it the de facto legislator on top of the other roles it already has. All this is made worse by the fact that the EU courts have, at best, played the role of a supporter in cartel-fining cases. The Commission’s work has, for the most part, been rubber-stamped by them.

It is therefore not surprising that Philip Lowe, in addressing due process issues, is taking cover behind the EU courts. Does this make his case more convincing? It does not, since the ultimate benchmark for due process standards lies outside the EU courts. It is the "European Convention for the Protection of Human Rights and Fundamental Freedoms" ("ECHR"). Even though the EU is not (yet) a party to this fundamental treaty, it is recognized by EU courts as an important lodestar in all questions of due process and the rule of law.

This might explain why Philip Lowe is bending over backwards to argue that the Commission’s fines are not of a criminal nature. However, there can be little question that the Commission’s record fines fall squarely within the definition of "criminal sanctions” enunciated by the European Court of Human Rights. This has, of course, wide repercussions for the procedural set up in cartel fining cases. Perhaps most important are the following:

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5 This also shows in the fact that the Commission has repeatedly emphasized the significant contribution the corporate cartel fines are making to the EU’s overall budget; cf. Press Release Commission, 21. November 2001, IP/01/1625, 3; NEELIE KROES, Car Glass Cartel, Opening remarks at press conference, Brussels, 12th November 2008, SPEECH/08/604, 3.

6 Cf. e.g. the amount of annual cartel fines in the US vs. the EU:

7 Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003, OJ C 210, 1.09.2006, 2-5.

8 Cf. SCHWARZE/BECHTOLD/BOSCH, Deficiencies (note 2), 14; SCHWARZE, Rechtssstaatliche Defizite (note 2), 9; SLATER/THOMAS/WAELBROECK, Law proceedings (note 2), 3.

9 Cf. SCHWARZE/BECHTOLD/BOSCH, Deficiencies (note 2), 61 et seq.; SLATER/THOMAS/WAELBROECK, Law proceedings (note 2), 7 et seq. There has been a recent attempt by a member of the Commission’s Legal Services to argue that the EU’s corporate cartel fines do, pursuant to the case law of the European Court of Human Rights, not belong to the category of “hard core” criminal law violations; cf. WOUTER P.J. WILS, The Increased Level of EU Antitrust Fines, Judicial Review, and the European Convention on Human Rights, available at...
• *Separation of Powers:* The artificial and merely internal separation of powers between the staff of DG COMP as prosecutors and the Commission as judge will, contrary to what Mr. Lowe suggests, not pass the test of the ECHR. Art. 6 calls for a clean separation between prosecutorial and adjudicating functions. The fact that the European Court of First Instance ("CFI") has, at least theoretically, unlimited discretion to judge all facts and legal questions in cartel fining cases, is of no help either. The European Court of Human Rights has stated repeatedly that, other than for "minor offences," the independence requirement applies to the first judicial body already.\(^{10}\)

• *Sec. 23 of Reg. 1/2003:* The vagueness of this provision violates the requirement of *nulla poena sine lege certa* (i.e. the need for a "clear and unambiguous legal basis"), as embodied in the ECHR.\(^{11}\) The only criteria mentioned in Sec. 23(3) Reg. 1/2003 for fixing the amount of fines are the "gravity and duration" of the infringement. These parameters are clearly not specific enough to justify fines in the amounts of several hundred millions of Euros or more. In addition, Sec. 23(2) determines that the maximum amount of the fine shall not exceed 10 percent of the total turnover generated by the relevant "undertaking." The term "undertaking" is likewise not specific enough as the Commission’s practice of applying it to whole corporate groups has shown.\(^{12}\)

• *Evidence Procedure:* Apart from the insufficient separation of powers, the corporations that are being subjected to cartel fines do not even have a right to be heard before any Commissioner, let alone the Commission as a whole. In fact, the only persons such corporations will typically meet during a procedure are the case handlers within DG COMP.\(^{13}\) This is a blatant violation of the ECHR. Sec. 6 grants each accused the right "to examine or have examined witnesses against him."\(^{14}\) Yet never, ever will it, for example, happen that a leniency witness has to appear before the Commission and the relevant parties in order to repeat his or her statements under oath. There is accordingly no way to cross-examine such witnesses even though they represent the most important evidence used in cartel cases. This is all the more disturbing given the distorted incentives such leniency witnesses could have: exaggerating the facts has no

\(^{10}\) Cf. SCHWARZE/BECHTOLD/BOSCH, *Deficiencies* (note 2), 60; SLATER/THOMAS/WAELBROECK, *Law proceedings* (note 2), 26 et seq. Cartel fines of the sort and magnitude imposed by the Commission do not qualify for an exception; cf. supra note 9.


\(^{12}\) Cf. infra VI.

\(^{13}\) Even though corporations also have a right to a formal hearing before a hearing officer, this right is often waived because of its mere token nature. In addition, no Commission member ever attends such a hearing.

\(^{14}\) KARSTEN GADE, *Fairness* (note 9), 274 et seq.
repercussions for themselves, but may protect their companies against broader allegations by others.\textsuperscript{15}

- \textit{Role of the EU Courts:} It is of little help that the CFI would theoretically have unlimited jurisdiction over cartel fining cases.\textsuperscript{16} First of all, even if the Court adjudicated each case from scratch, this would not satisfy the requirements of the ECHR. Second, the CFI exercises, in practice, a mere plausibility control of the cases decided by the Commission. It thereby corroborates the deficiencies in the EU’s cartel fining procedures by giving them the apparent blessing of a seemingly independent fully fledged judicial review.\textsuperscript{17}

\section*{III. FIGHTING CARTELS EFFECTIVELY}

Due process issues aside, Philip Lowe leaves no doubt that he considers the Commission’s current enforcement system to have been a tremendous success. His conclusion: "Companies are finally taking antitrust violations in Europe seriously."

Mr. Lowe then goes on to emphasize that the “enormous economic harm caused by cartels” explains why:

The Commission pursues a zero tolerance policy vis à vis this type of infringement. Fines have two objectives. First, fines serve to punish the perpetrators. Second, and perhaps even more importantly, fines have a deterrent effect by discouraging other companies from continuing or entering into anticompetitive practices. Sufficiency deterrent fines therefore constitute the lynchpin of a successful competition policy.\textsuperscript{18}

What Mr. Lowe says in principle is hardly controversial. The problem is that he misses the point. The issue is not whether fines are justified as such. The issue is which amounts of fines or other sanctions are justified against whom and for what? It is here where the

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\textsuperscript{15} Schwarze, Kartellbussgelder (note 2), 192 et seq.
\textsuperscript{16} Cf. Schwarze/Bechold/Bosch, Deficiencies (note 2), 59 et seq.; Schwarze, Kartellbussgelder (note 2), 185 et seq.; Slater/Thomas/Waelbroeck, Law proceedings (note 2), 43 et seq.
\textsuperscript{17} The situation in the EU contrasts drastically with the due process system in the United States. Christine Varney, the Assistant Attorney General and head of the Antitrust Division of the U.S. Department of Justice, recently described the rule of law standards built into the U.S. antitrust enforcement system as follows: Finally, I will briefly sketch the judicial process that is triggered once the Division brings an enforcement action. As I alluded to before, the Division cannot unilaterally order parties to take or not take certain actions. Instead, we must bring an action in court to obtain relief. In our court system, neutral judges who have no connection to the Antitrust Division are tasked with deciding disputed issues of fact and assessing the soundness of our legal theories. Among other important functions, judges rule on evidentiary disputes, assess witness credibility, and decide contested issues of fact. In a public proceeding, parties are given full opportunity to contest our evidence, submit their own evidence, and advance their own interpretation of the law. Court proceedings are governed by the Federal Rules of Civil Procedure and the Federal Rules of Evidence, which are available to everyone and provide quite detailed instructions about the course of a litigation and the kinds of evidence that can be considered. A trial court’s decision is made publicly, and it is subject to further review through our courts of appeals and, potentially, our Supreme Court;\textsuperscript{18}

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Commission’s deterrence concept starts to fail. Instead of indiscriminately imposing fines on corporate groups for cartel violations which happened anywhere within these organizations, a legally and economically sound sanctioning policy would require differentiations along three dimensions:

- the corporate governance dimension, calling for a separation between the responsibilities of a corporation and the individuals acting for it;
- the fault dimension, requiring a clear notion of fault for corporate organizations;
- the corporate group law dimension, differentiating between the responsibilities of parent companies and those of the subsidiaries where the cartel violations happened.

IV. RECOGNIZING THE AGENCY PROBLEM

Fines have a purpose—and they certainly should have one. The Commission has said repeatedly that deterrence is the overriding goal of cartel fines.\(^{19}\) Philip Lowe confirms this in his article. He is right. Cartel fines should mainly aim at deterring companies and managers from cartelizing in the future. The problem is that EU fines are directed against companies and therefore paid by shareholders. Deterrence, on the other hand, should mainly be targeting those who are responsible for the cartel conduct, i.e. the managers. How does the Commission solve this conundrum? It doesn’t. By ignoring the fundamental "agency problem" in modern corporate governance, i.e. the fact that managers and shareholders do not always have congruent agendas, the Commission’s fining concept targets shareholders only. Does this matter? It sure does.

By giving the managers who are responsible for cartel conduct a free ride, the Commission’s fining policies can never be fully effective, no matter how excessive corporate fines may be. Of course, the companies can dismiss managers who had been involved in cartel conduct. The company can even sue them for damages. Yet, there are at least two problems with this. First of all, the Commission’s leniency policies force companies into a rat race once they have indications about past cartel conduct. This might compel them to waive potential rights against such managers in order to cause them to talk. Second, and partially as a consequence, the potential company sanctions a manager has to realistically reckon with might easily be outweighed by the temptations of improving his management results through cartel arrangements. The only really effective threat for such managers would therefore be individual criminal sanctions.

EU cartel law does not, at least so far, provide for the use of criminal law against individuals, even though this would be in line with international trends. Philip Lowe justifies the EU’s position with the following arguments:

There is little doubt that criminal sanctions generally have a significant deterrent effect on individuals. At the same time, deterrence resulting from criminal sanctions has its limits as a quick glance into any local newspaper will confirm. In addition, and leaving aside the disputed question of the existence of a legal

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19 Cf. NEELIE KROES, Tackling cartels – a never ending task, Brasilia, 8\(^{t}\)h November 2009, SPEECH/09/454, 4 et seq.; KROES, Antitrust (note 3), 3.
basis and political feasibility, criminalization would require a complete overhaul of the Commission's investigative powers and procedures and not least the creation of a European criminal court.\textsuperscript{20}

As the European Court of Justice ("ECJ") has held, criminal law sanctions can be mandated on member states as an auxiliary measure to prop up the implementation of EU policies.\textsuperscript{21} This shows once more: where there is a will there is a way. It is obvious, however, that the Commission has not had a serious interest in questioning the effectiveness of its "corporate fines only" cartel policies. This may be understandable if one looks at the discretion the Commission enjoys in setting fines and the limited checks and balances under which it operates.\textsuperscript{22} But it in no way excuses the Commission's lack of interest in trying to improve the effectiveness and fairness of the current cartel fining laws.

V. RECOGNIZING CORPORATE FAULT

Deterrence can only work if its target has the ability to change things for the better. There is only so much a company, i.e. its shareholders and top management, can do to prevent cartel violations by individual perpetrators. Where top management is involved in the cartel conduct, the function of sanctions is to deter top management itself from cartelizing. In this case, a legal argument could be made that punishing the company is justified because top management is the very representative of the company. Functionally, it could be argued that top management can be monitored relatively closely by shareholders. Illegal conduct by top management therefore could be said to indicate a lack of supervision on the part of shareholders. Hence, company fines could arguably improve shareholder oversight.

As tenuous as this argument might sound in the context of large public corporations, applying it to any employee within a company is all but absurd. It is commonplace to say that modern global corporations are highly complex and that there is no way to control and monitor everything employees are doing. The consequences of this truism are real, however. Shareholders, who ultimately pay large corporate fines, have only limited means at their disposal to influence employee conduct. In principle, all they can do is put in charge capable top management that, in turn, implements the best possible compliance organization. To the extent that this is not happening, fines against companies can be justified. They serve as an incentive to develop, introduce, and enforce best practice compliance.\textsuperscript{23}

The legal upshot of this is that making companies strictly liable for illegal cartel activities by any of their employees is dysfunctional. Rather, what is needed is a fault-based liability system that punishes companies (and hence their shareholders) for what they can influence and change \textit{ex ante}. This leads straight to best practice compliance as the litmus test for every

\textsuperscript{20} LOWE, Cartels (note 4), 6 et seq.


\textsuperscript{22} Cf. supra II.

\textsuperscript{23} The requirements for best practice compliance could, e.g., affect the following areas: Rules/Procedures, Supervision/Responsibility for implementation, Training/Instruction, Recruitment/Filling positions of responsibility, Audits/Protection of whistleblowers, Implementation/Sanctions, Risk mapping/Adapting compliance measures; cf. HOFSTETTER/LUDESCHER, Parent Companies (note 2), 9 et seq.
corporate cartel fine. Put differently, corporate cartel fines ought to reflect the failure of companies to implement best practice compliance measures. The closer a company comes to this best practice standard, the lower the fine should be and the other way around. It is obvious, of course, that the cartel violations as such can be no obstacle to prove the implementation of best practice compliance. Compliance measures, even of the highest standard, are no guarantee that cartel violations won’t happen. However, they are the only means for companies to contribute to the prevention of cartel activities. Everything else is beyond their power and thus also beyond the deterrent effect of corporate fines.24

In stark contrast to this real-world deterrence concept, the Commission’s cartel fining policy is based on the notion that companies are strictly liable for the cartel conduct of any of their employees. This also flies in the face of Sec. 23 of Reg. 1/2003, which explicitly provides for a fault standard to be applied. Fines shall be imposed if companies engaged intentionally or negligently in cartel activity. This has so far been overlooked by the Commission and the Community courts. It is therefore high time to close the conceptual loop and to bring together the functional concept of corporate cartel fines with the legal basis providing for them. The result would be corporate fines that are not only a reflection of the harm caused by cartel activities, but also a reflection of organizational fault, i.e. the failure to implement best practice compliance.25

VI. CALIBRATING PARENT COMPANY FAULT

A third major deficiency of the EU’s current cartel fining policies from both a legal and functional point of view is its failure to properly recognize the boundaries between parent companies and their subsidiaries. In his article, Philip Lowe glosses over this issue, even though it is a major factor in explaining why the Commission’s fining policies have been spinning out of control.

The current practice of the European Commission is characterized by the view that the parent company must ultimately assume full responsibility for all antitrust violations committed within a corporate group. Ignoring the fundamental concept of limited liability for

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24 The elimination of illegal gains should, according to the Commission, be achieved by means of civil claims brought by the injured parties and not through fines. Cf. for example European Commission, staff working paper: EC antitrust damages actions, 10.2.2006, 7; European Commission, White Paper: Damages actions for breach of the EC antitrust rules, 2.4.2008, 3. If fines were having that function too, they would have to be based on the damages caused. However, this is by no means the case in the current fining policies of the Commission; cf. HOFSTETTER/LUDESCHER, Parent Companies (note 2), 17 et seq.

25 The following fine formula, which was developed in HOFSTETTER/LUDESCHER, Parent Companies (note 2), 17 et seq., could be used for that purpose:

$Fine = \frac{CoC - CaC}{LD} + \left( \frac{CoC - CaC}{CoC} \times ICR \right) - pCC$

CoC = Costs of optimal compliance
CaC = Costs of actual compliance
LD = Likelihood of discovery
ICR = likely cartel profits
pCC = probable civil claims
subsidiary corporations, the Commission espouses a system of “guilt by association.” Parent companies are, in other words, made co-liable for cartel violations by subsidiaries even though they might not have been aware of them at all. Worse, the Commission does not even check whether the parent company had any way to learn about these violations or prevent them. This is in contradiction to the fault principle laid out in Art. 23 of Reg. 1/2003. The only prerequisite the Commission recognizes for making the parent jointly and severally liable with a subsidiary is the general influence the parent had over the latter’s “commercial policies.” This is taken to mean that the subsidiary "did not determine its conduct on the market independently." In practice, this is always presumed to be the case.

To be sure, the purpose of the Commission’s corporate group approach is not to establish the parent’s co-liability as such. The real purpose is to raise the fine cap in Sec. 23 Reg. 1/2003 to 10 percent of group sales. This typically results in a huge expansion of the Commission’s discretion in determining the amount of the fine.

The EU courts have, admittedly, not (yet) stopped the Commission on its ill-fated course. The recent Akzo Nobel decision, too, was not particularly constructive in this regard. By upholding the CFI’s confirmation of the parent company’s co-responsibility, the ECJ gave conflicting messages. On the one hand, it brushed aside Akzo Nobel’s attempt to clearly separate the responsibilities of different legal entities within a corporate group. On the other, the Court almost went out of its own way to emphasize that such co-responsibility is not "strict.”

By rejecting the notion of strict parent company liability, the ECJ, in fact, opened up a Pandora’s box. The only alternative to strict liability is fault-based liability. The court, however, gave no guidance on how the parent’s fault would have to be gauged. Is interfering with the market conduct of a subsidiary itself a fault? Or is it rather a question of how this market conduct is being influenced? Would the implementation of "Best Practice Compliance” be sufficient to rebut fault? The ECJ’s Akzo Nobel decision remains silent on all these crucial questions.

Parent company liability for cartel violations of subsidiaries can be legitimate from both a legal and functional point of view. A parent assumes responsibility through the faults of its own directors and officers. Proof of the latter’s intent or negligence would therefore be the way to attach liability to the parent. Negligence could be construed if the parent’s board or management had not properly imposed best practice compliance measures on the subsidiary.

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27 ECJ, 10.9.2009, Akzo Nobel NV et al./Commission, Case C-97/08 P, margin no. 72 et seq.

28 ECJ, 10.9.2009, Akzo Nobel NV et al./Commission, Case C-97/08 P, margin no. 77.

29 This is confirmed by the German translation of the judgement which talks of "verschuldensunabhängige Haftung"; ECJ, 10.9.2009, Akzo Nobel NV et al./Commission, Case C-97/08 P, margin no. 77.
even though the parent had an obligation to do so. Does and should such an obligation exist at all?

If the parent company exerts direct influence over the operating activities of the subsidiary, e.g. its sales and marketing departments, there are sound legal and economic reasons to demand that it put in place adequate compliance systems. By directly controlling areas in which antitrust violations can occur, the parent voluntarily assumes the role of a guardian. It is therefore properly positioned to monitor the subsidiary’s compliance with cartel law.

The fact that the parent company intervenes in the market conduct of its subsidiary could furthermore be justification for shifting the burden of proof. It could be argued that the parent should be required to prove that it had implemented best practice compliance structures and policies at the subsidiary.

However, if the exertion of influence is restricted to laying down strategic plans and financial targets, the connection to an infringement of competition law is not strong enough to presume that the parent acted negligently. In other words, merely setting strategic and financial targets for the subsidiary does not in and of itself justify reversing the burden of proof with regard to the implementation of a proper compliance system. In such a scenario, it would therefore be up to the Commission to prove, as essentially provided for in Sec. 23(2) Regulation No. 1/2003, that the parent company acted negligently by not implementing a proper compliance system at the subsidiary.30

VII. CONCLUSION

Contrary to Philip Lowe’s assessment, the EU’s cartel fining laws and policies are in a highly questionable state: basic principles of due process are being violated; corporate governance realities are being ignored; the fault principle is being disregarded; and the limited liability of corporations, a bedrock of modern business law, is being sidelined.

Radical change is needed. Yet there is only one area where a dim light is flickering at the end of the Commission’s tunnel. In his article, Philip Lowe asks the question: "Should compliance programs be rewarded with a reduction in fines?" His answer shows at least lukewarm openness:

This is a difficult question. The Commission certainly welcomes compliance programs as a useful tool for companies, to help prevent and deter antitrust infringements. On the other hand, companies are obliged by law to comply with competition rules and compliance programs form a part of standard corporate governance. The debate on this issue will continue.

Paying lip service to debates is one thing. Engaging in the full substance of a debate and making real strides towards policy changes is another. Yet, little can apparently be expected

30 Cf. HOFSTETTER/LUDESCHER, Parent Companies (note 2), 6 et seq.
from the outgoing Commission in that regard. It is telling that Lowe’s article ends by coming full circle: "Fines should not be expected to decrease anytime soon."  

Where to go from here? One hopes that the new Commission will take office with a more open, less defensive frame of mind. In addition, there is the prospect that EU courts might finally take serious their task as the guarantors of due process and the rule of law in the area of cartel law enforcement. Once the EU joins the ECHR, the European Court of Human Rights can be expected to step in, too. Last but not least, the EU legislature has an opportunity to amend Reg. 1/2003 in connection with the current review process. Reform must come and reform will come.

31 Lowe, Cartels (note 4), 7.