

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

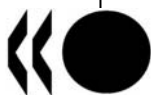
ROUNDTABLE ON PROMOTING COMPLIANCE WITH COMPETITION LAW

-- Note by the Delegation of Germany --

This note is submitted by the delegation of Germany to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 29-30 June 2011.

JT03304252

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1. Introduction

1. Over the last years, the Bundeskartellamt has stepped up its enforcement of the ban on cartels, often leading to heavy fines. This shift of focus to cartel enforcement has gone hand in hand with a heightened awareness within the business community for competition law compliance. This paper focuses on compliance issues in the area of cartel prohibition. Compliance, in this context, is to be understood as adherence to the relevant provisions of competition law. The paper will give an overview of the determinants of compliance (B.), will then turn to the options for a competition authority for promoting compliance (C.) and will finally touch upon corporate compliance programmes (D.).

2. Determinants of compliance

2. The decision of companies whether to comply with existing competition law may look like a simple choice of risk vs. reward. In reality the decision is much more complex, involving an array of factors that determine the degree of compliance of a company.

3. For companies and individuals, the following determinants may be the most influential: (1) Knowledge of the law, (2) Social motivation, (3) Risk/reward.

2.1 Knowledge and awareness

4. Compliance requires knowledge of the law and the rules to comply with. Rules on hardcore infringements of competition law tend to be known by all market participants concerned, and there is hardly any confusion about, e.g., price fixing being a serious infringement. However, knowledge about other hardcore infringements, e.g. some forms of information exchange, may be less widespread. Especially smaller companies without specialised law departments or resources to hire external experts on a constant basis, might have a knowledge deficit. This is where competition advocacy has an important role to play, as will be described in more detail below.

5. There may be a gap between the company's institutional knowledge of competition law and that of individuals within the firm, especially if the company's knowledge is kept within the legal department. Whether and to what extent the knowledge is spread within the company depends on the company culture and any corporate compliance programme. An efficient compliance programme, thus, needs to comprise the regular instruction of company representatives in critical areas, such as sales.

2.2 Social motivation

6. Compliance requires knowledge of the rules and the willingness to comply, in order to avoid any conflict with the law. Compliance may be further facilitated by an appropriate company culture that communicates abiding by the law as a cornerstone of company policy to the wider public. For example, after going through extensive corruption investigations which generated negative press coverage, several

German companies have recently made substantial investments into their compliance policies and have actively advertised their new image to the public.

7. The nexus of the “culture of compliance” within a company with public opinion is not to be discounted. Compliance is likely to be high if public opinion judges infringements of competition law to be serious offences.

8. The social context is also an important factor for compliance in the behaviour of individuals. If infringing competition law entails social consequences, compliance is more likely. Social pressure imposed within the company is of particular importance. The management and stakeholders of a company are responsible for creating an environment in the company in which cartel infringements are not tolerated.

2.3 Risk/Reward

9. From an economic point of view, companies following a profit-maximizing strategy will organize their activities based on a risk-reward-scheme to determine overall profits. The profits resulting from a cartel are determined by three main factors: expected cartel gains, consequences, esp. fines, in case of detection, and detection risk.

2.3.1 Expected cartel gain

10. From the point of the firm, the advantage to be expected from a cartel is an important determinant of compliance. The higher the expected gain, the more tempting it is to ignore competition law.

11. Although employees of the firm may not profit directly from a cartel offence, they may benefit from indirect or even unintended incentives a company sets, e.g. bonuses and promotions. Salary systems that operate with large bonus components for turnover / profit increases may inadvertently tempt managers or employees to infringe competition law. This is particularly problematic if those bonuses are not tied to the condition of compliance, i.e. cannot be recalled if it turns out later that the individual generated the extra profit by infringing competition law.

2.3.2 Sanctions and other negative consequences

12. Negative consequences for a company of not complying with competition law can be: Monetary sanctions/administrative fines; reputation loss; civil damage claims; and negative stock market reaction (often this may be a result of the three previous factors). Substantial fines for infringements may be necessary to make compliance with the law the best outcome of a company’s risk-reward-deliberation.

13. Consequences in case of detection for individuals may be external or internal in nature. “External” consequences include the sanctions imposed by the authorities, such as fines on the individual, but also loss of reputation. For example, managers having infringed competition law may in some cases not be seen as suitable to lead a company. “Internal” consequences set by the corporation/employer may be the reclaim of relevant bonuses; civil damage claims by the employer; severe consequences for the career track; or the loss of reputation within the corporation.

2.3.3 Detection risk

14. The risk of detection is of key importance for compliance: the higher the detection risk, the greater the weight of the possible negative consequences of detection in the internal risk calculation of a firm weighing the pros and cons of participating in a cartel. Effective cartel prosecution by a competition authority is an important factor for raising the risk of detection.

15. Individuals face not only the “outside” detection risk (i.e. by competition authorities), but also an “inside” detection risk (i.e. by colleagues, superiors or the company’s own compliance officers). Whether this inside detection risk is a serious threat depends largely on company culture and the implementation of an effective compliance programme.

3. Promoting compliance as a competition authority

16. The primary approach of a competition authority to increase compliance with the prohibition on cartels is arguably to step up prosecution to alter the risk- benefit calculation of the companies. While this is central other tools should not be neglected. Gaining a good understanding of critical markets, raising awareness among market participants for problematic structures in that market and working towards modifying them can play an important role.

17. Cartel-prone markets, in the experience of the Bundeskartellamt, are those with few participants and homogenous goods, such as certain construction materials. Some of these markets in Germany are characterized by numerous joint ventures which may have further facilitated stable collusion. The Bundeskartellamt pays close attention to structural conditions in these markets, e.g. via merger control, administrative cartel proceedings as well as sector inquiries. These may result in the cutting of ties between market players which might keep them from competing.

18. It remains unclear whether the increase in the number of cartels detected over the past years corresponds to an increased number of cartel agreements. It is possible that due to cartel prosecution becoming more effective, more cartels are uncovered while at the same time the number of undetected cartels becomes smaller. It is, however, safe to say that three elements are essential for the effective promotion of compliance: competition advocacy, deterrence in the form of severe sanctions and high detection rates.

3.1 *Competition advocacy: Awareness and guidance*

19. Competition advocacy is an essential part of promoting compliance and involves creating awareness and giving guidance to the public. Competition advocacy increases the knowledge of the stakeholders of competition law and strengthens the competition culture. Furthermore, it helps increase awareness among the public and promotes public support for the work and task of the competition authority.

20. Competition advocacy is multifaceted. The Bundeskartellamt strives to reach out not only to lawyers and economic experts but also to employees and citizens.

21. Besides the key tools of general advocacy (e.g., guidance on the law; publications on cases; press relations), the following measures may be of particular relevance for advocacy in fighting cartels:

- Providing a hotline and a mailbox for citizens’ complaints;
- Publication of sector studies;
- Close cooperation with other public institutions (e.g. ministries, courts, state prosecutors).

3.2 *Deterrence*

22. From a theoretical point of view, effective deterrence requires that the “sanctions and other negative consequences” multiplied with the “detection risk” exceed the “expected cartel gain”.

23. In Germany the fines imposed on companies convicted of a cartel offence are based upon the relevant legal provision¹ and the Bundeskartellamt's fining guidelines.² The amount of a fine imposed on a company for a cartel offense can reach up to 10 per cent of the company's total turnover. In practice, the fine for a hardcore offense usually corresponds to 15-30% of the cartelised product turnover of the cartel member.

24. Individuals directly or indirectly (i.e., via a breach of the duty to supervise their employees) involved in the cartel may be fined up to 1 million euros. Criminal sanctions are only relevant for individuals involved in bid rigging (usually fines, not jail sentences).

25. Press relations are crucial for competition advocacy, and also play a role in deterrence. Companies are aware of the risk of loss of reputation if the public learns of a cartel infringement. Publicity from a cartel case may also raise the awareness of potential civil damage claimants.

26. The duration of a cartel proceeding is relevant in its own right. In Germany, the length of the proceeding is a mitigating factor when it comes to calculating the appropriate fines. Lengthy proceedings bind resources of the enforcement authorities which might be used for other cases. Therefore shorter proceedings allow for higher fines and more proceedings, resulting in more deterrence.

27. The Bundeskartellamt tries to identify factors influencing the duration of a proceeding:

- According to former German law the maximum amount of a fine for a cartel infringement of a company was three times the illicit gain of the cartel offence. Due to the high standards of the courts the proof of the illicit gain and therefore the calculation of the fine required time-consuming investigations with respect to the necessary data and complex calculations of economic experts. These results were often disputed, even when the cartel offence itself was obvious. The German law has since been adjusted to the current fining standard based on company turnover bringing it into line with European fining rules.³ This promises to reduce the scope of arduous and time-consuming discussions over illicit gains.
- Settlements can avoid lengthy court proceedings and free resources for other cases. The Bundeskartellamt is therefore open to settlements and has further streamlined its settlement proceedings in recent years.⁴ Since the beginning of 2007 the Bundeskartellamt has reached settlement decisions in circa 80% of its proceedings (with at least one cartel member), with circa 65% of the companies fined since 2007 and in respect of circa 40% of the total amount of the fines imposed on companies since 2007.

3.3 *Effective detection instruments*

28. The Bundeskartellamt has a wide array of detection instruments and mechanisms at hand to increase the detection risk of companies and thus foster compliance. Detection in this respect not only comprises uncovering a cartel, but also uncovering and collecting all evidence necessary to prove the infringement:

¹ Section 81 Act Against Restraints of Competition (ARC). An English version of the ARC is available at http://www.bundeskartellamt.de/wEnglisch/download/pdf/GWB/0712_GWB_mitInhaltsverzeichnis_E.pdf.

² http://www.bundeskartellamt.de/wEnglisch/download/pdf/Merkblaetter/Bussgeldleitlinien-E_Logo.pdf.

³ http://www.bundeskartellamt.de/wEnglisch/download/pdf/Merkblaetter/Bussgeldleitlinien-E_Logo.pdf.

⁴ C.f.: http://www.bundeskartellamt.de/wEnglisch/download/pdf/Fallberichte/B11-018-08-Kafferoester_engl.pdf?navid=31.

- **Leniency programmes:** Leniency programmes have become a centre piece among the Bundeskartellamt's detection instruments. In 2010, the Bundeskartellamt received 56 applications concerning 25 different cases.
- **Other sources:** A significant number of cases⁵ are detected on the basis of sources other than leniency applications such as complaints and hints from other market participants, (ex)employees of cartel members and information from other cases (e.g. merger control cases) which are often combined with market observations e.g. via internet research or sector inquiries.
- **International cooperation:** Working closely together with other competition authorities can help uncover cartels. Sometimes parallel cartels are formed in different countries, so information about the cartel investigations in the neighbouring countries can be helpful.
- **Cooperation with non-competition authorities:** In addition to international cooperation between competition authorities, the Bundeskartellamt has cooperated with various non-competition authorities, such as state prosecutors or financial authorities.
- **Dawn raids:** Dawn raids are one of the Bundeskartellamt's most important tools for finding and securing detailed information about a cartel. In 2010 the Bundeskartellamt conducted dawn raids in 15 cases. In the Bundeskartellamt, a Special Unit for Combating Cartels organises these dawn raids, keeps contact with police and state prosecutors and secures an efficient procedure.
- **Witness interviews:** Witness interviews serve to secure and prepare material for assessing whether there has been an offense, and for proving it in authority proceedings and in court. The Bundeskartellamt has significantly strengthened its expertise in conducting witness interviews by working with police and public prosecution experts.
- **IT search and evaluation:** IT evidence is becoming more and more important. The Bundeskartellamt has therefore created a specialist unit for securing and preparing IT evidence with the aim of uncovering incriminating evidence and proving the alleged cartel.

4. Corporate compliance programmes

29. Corporate compliance programmes can be very conducive to overall compliance. Ideally every company should have a compliance policy that minimizes the risk of its managers or employees participating in cartel agreements.

30. It is the task of the companies to develop compliance programmes that are effective in the special context of their business. The Bundeskartellamt refrains from providing any kind of check list that automatically qualifies a programme as effective, since this might actually be counter-productive. The Bundeskartellamt is aware of the risk that, based on such a check list proposals in formal terms while not enforcing them in practice. Compliance programmes should contain the same elements as the policies of the competition authorities when promoting compliance with competition law: guidance, detection and sanctions. These elements can be tailored by the companies to their particular industry and their own specific needs.

31. The company is best placed to get the message of compliance across to its employees and managers, e.g. by making sure that the sanctions for infringing competition law or for tolerating an infringement by others exceed the incentives to commit offences. The company is also well placed to detect any infringements, e.g., by regular due diligence, internal whistleblower hotlines or unannounced controls.

⁵ Of the cases fined in 2010: three out of eight.

32. However, the mere existence of a corporate compliance programme is a neutral factor for determining the amount of fines and does not warrant reductions. Compliance is a legal obligation of undertakings – company law requires firms to make compliance efforts - and there can be no reward for not observing the law.

33. Nonetheless, effective corporate compliance programmes bring large rewards for the undertakings. The rewards increase with the efficiency of the programme. They can be summarized as follows:

- Well-designed and implemented compliance programmes will prevent infringements before they take place. This will save the company fines, the compensation of civil damage claims and reputation losses.
- Compliance programmes will not always prevent infringement. But if they are effective they will at least help to uncover the infringement faster than the competitors. According to the German leniency programme⁶ which is based on the ECN Leniency Model Programme, this allows the company to attain first place in the leniency queue and therewith a 100% reduction of the fine.
- Even after a dawn raid an efficient compliance programme can help to obtain a substantial reduction of the fine for providing information and applying for leniency. The faster the company can gather the necessary information internally with the help of the compliance programme, the higher the reduction can be (up to 50%).
- Finally, a settlement is probably easier to achieve for the company because the company will know its current situation and thus its bargaining position due to the internal compliance investigations rather well.
- When it comes to a possible breach of supervisory duties, compliance programmes can be very helpful, too. An effective, “non-sham” compliance programme can fulfil of these very same duties and hence prevent fines resulting from the violation of supervisory duties.

⁶

<http://www.bundeskartellamt.de/wEnglisch/FurtherInfo/leniencyW3DnavidW2629.php>.