

Expert Analysis

Quantifying Antitrust Damages In Private Enforcement Actions Under European Union Competition Law

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As part of its continuing efforts to identify and address the obstacles to effective antitrust damages actions in the European Union in December 2009, the European Commission released the report "Quantifying Antitrust Damages: Toward Non-Binding Guidance for Courts," hereafter referred to as "the report."¹ The report followed on the heels of the EC's "White Paper on Damages Actions for Breach of the EC Antitrust Rules," adopted April 2, 2008,² and "Green Paper on Damages actions for Breach of the EC Antitrust Rules," adopted Dec. 19, 2005.³

The purpose of the Green Paper and the accompanying staff working paper⁴ was to identify the main encumbrances to a more effective system of antitrust damages claims and to set out options to improve antitrust actions brought within the EU. The White Paper and the accompanying staff working paper⁵ were prepared for the primary objective of providing detailed proposals for improving the legal conditions for victims of breaches of antitrust laws under Articles 81 and 82 of the EC Treaty to exercise their rights to seek reparation for their damages.

The White Paper identified the quantification of damages as one of the impediments to damages actions. It noted there was wide support for the suggestion in the Green Paper for further guidance on the calculation of antitrust damages. Toward that end, the EC commissioned a study to assist it in the formulation of a framework, the objective of which is "to provide pragmatic, nonbinding assistance in the difficult task of quantifying damages in antitrust cases, both for the benefit of national courts and the parties."⁶ The EC-commissioned report is the result of the EC's desire to develop such guidance. It represents the "next step" in the European policy debate on private damages actions.

THE WHITE PAPER: AN IMPORTANT BACKDROP TO THE REPORT

The White Paper laid the groundwork on the current state of the law and policy on antitrust damages in the EU, which ultimately shaped the scope of the report. It emphasized the following main principle behind damages claims as established in EU antitrust case law:

Any citizen or business who suffers harm as a result of the breach of EC antitrust rules (Articles 81 and 82 of the EC Treaty [now Articles 101 and 102 TFEU]) must be able to claim reparation from the party who caused the damage. This right of victims to compensation is guaranteed by Community law, as the European Court of Justice recalled in 2001 and 2006.⁷

Importantly, with respect to antitrust damages, the EC confirmed in the White Paper that “[f]ull compensation is ... the first and foremost guiding principle.”⁸ The White Paper also recognized that “[e]ffective remedies for private parties also increase the likelihood that a greater number of illegal restrictions of competition will be detected and that the infringers will be held liable. Improving compensatory justice would therefore inherently also produce beneficial effects in terms of deterrence of future infringements and greater compliance with EC antitrust rules.”⁹

The commission determined that there existed an extensive *acquis communautaire*, or body of law, on the definition of antitrust damages in the EU, which it suggested be codified. In general the European Court of Justice has ruled that as to the scope of damages that victims of antitrust infringements can recover, victims must receive, at a minimum, full compensation of the real value of the lost suffered, extending not only to actual losses, but also lost profit and a right to interest.

The existing *acquis communautaire* on antitrust damages in the EU, among other things, was discussed more fully in the staff working paper that accompanied the White Paper. The main principles can be summarized as follows:

- Victims of an infringement of EC competition law are entitled to full compensation of the harm caused. That means compensation for actual loss (*damnum emergens*) and for loss of profit (*lucrum cessans*), plus interest from the time the damage occurred until the capital sum awarded is actually paid.
- Victims of an EC competition-law infringement are entitled to particular damages, such as exemplary or punitive damages, if and to the extent such damages may be awarded pursuant to actions founded on the infringement of national-competition law.
- In the absence of Community law on the matter, member states are allowed to take steps to ensure that the protection of the right to claim damages for the loss caused by a competition-law infringement does not entail the unjust enrichment of the victims.¹⁰

As to the calculation of antitrust damages, the EC also looked to the *acquis communautaire*. It found one general rule: “The principle of full compensation implies that member states may not *a priori* fix any form of upper limit of the amount of compensation that the victim of a competition-law infringement could effectively recover.”¹¹

The commission also determined that, pursuant to the case law of the Court of Justice, in the absence of any further community rules concerning the calculation of damages, it is for the domestic legal system of each member state to determine what a claimant must prove with respect to the amount of damages he has suffered and the methods that can be used in calculating the amount.

In addition the EC stated that domestic requirements cannot violate the principle of effectiveness, *i.e.*, they cannot render excessively difficult the exercise of rights conferred by EC law. Thus, it concluded that a national court is excluded from not awarding any damages simply because the claimant cannot prove with sufficient precision the amount of harm suffered.

The EC determined that while the scope of damages is more easily ascertainable, the quantum of damages is “often a very cumbersome exercise.”¹² It generally recognized the difficulties in determining damages where calculating the exact amount would be “excessively difficult or even practically impossible” versus a more far-reaching calculation that could result in an amount disproportionate to the actual amount of damages suffered.

Thus, the EC determined that in order to facilitate the calculation of damages, it intended to develop nonbinding guidance for quantification of antitrust damages, *e.g.*, by means of approximate methods of calculation or simplified rules on estimating the loss. The commissioning of the report was the answer to the call.

THE SCOPE AND STRUCTURE OF THE REPORT

The report was prepared for the EC’s Directorate-General for Competition by Oxera Consulting Ltd. with a multi-jurisdictional team of attorneys and economists. The study is rooted in a number of sources, including current academic literature and thinking in the areas of economics, corporate finance and modeling, competition-case law (including best practices in Europe and the United States), and the EC’s White Paper and surrounding policy debates.

Following the EC’s recommended aims, the study seeks to strike a balance between two differing objectives: the desire to determine the actual damage amount as closely as possible (in line with the EC’s “full compensation” principle) and the desire to remove obstacles to private damages actions through approaches that are clear and easy to apply.

The study focuses on the types of cases where damages actions are most likely to be brought: cartel infringements under TFEU Article 101 (with most weight on damages from cartel overcharges) and exclusionary abuses of dominance under Article 102. However, the report is intended to cover other types of damages in line with the principle that all victims of all types of antitrust infringements are entitled to compensation for the damages they suffered.

The report is structured into four main sections: Section 2 provides a conceptual framework for quantifying antitrust damages¹³, Section 3 classifies the various methods and models that can be used in quantifying damages¹⁴, Section 4 sets out further insights provided by economics and finance literature and legal precedent that can assist in deriving a damages estimate¹⁵, and Section 5 draws together Sections 2 to 4 and explains how one could effectively use methods and models together with the further insights to arrive at a final value of the damages calculation in line with the conceptual framework.¹⁶

SECTION 2 OF THE REPORT: CONCEPTUAL FRAMEWORK FOR DAMAGES CALCULATION

According to the report, the rationale for the conceptual framework for antitrust damages calculation is to place the victim back into the financial position that he would have been in but for the antitrust infringement. The report breaks down this framework into two main stages.

First, there should be an assessment of what would have happened in a hypothetical scenario where the infringement had not taken place. This is commonly referred to as the “but for” (U.S.) or “counterfactual” (EU) scenario and typically is the central stage in any damages estimation.

The European Court of Justice has ruled that, as to the scope of damages that victims of antitrust infringements can recover, victims must receive, at a minimum, full compensation of the real value of the lost suffered.

The report describes the determination of a counterfactual scenario as requiring a detailed review of several questions, including:

- What type of infringement (*e.g.*, cartel? exclusionary conduct?) is causing what type of harm (*e.g.*, overcharge? loss of sales?).
- What types of parties have been harmed (*e.g.*, direct purchasers? end consumers? competitors?).
- What is the nature of the market and/or industry in which the harm has arisen (*e.g.*, new? mature?).

Second, there must be a conversion of the difference between the factual and counterfactual scenarios to determine a final damages value.

The report further discusses the steps involved in developing an accurate counterfactual scenario. With respect to the types of antitrust infringements, it groups them into three categories under Articles 101 and 102:

- Horizontal price-fixing and market sharing.
- “Exploitive” abuses of dominance¹⁷
- “Exclusionary” abuses of dominance and vertical and horizontal agreements with exclusionary effects.

The report then identifies the types of harm arising from these various infringements.

With respect to price-fixing cartels, it describes the primary harm as higher prices. This is typically expressed as the cartel overcharge, or a percentage of the actual price. Another harm from a price-fixing cartel identified in the report is the “lost volume” effect or “deadweight welfare” loss. This represents an inefficiency to the economy as a whole. The report also recognizes the more difficult to quantify and prove harms of volume reduction and negative effects on quality.

In addition to price and quantity effects, the report also observes that cartels can have “longer-term effects on market structure and market functioning.”¹⁸ For example, it suggests that the “reduction in rivalry between firms can result in lower levels of innovation and a slowing-down in the rate at which improvements in efficiency are achieved or at which inefficient firms exit the market.”¹⁹ The report concludes that all these long-term effects may have to be taken into account in the damages calculation, since they may affect the counterfactual price.

With respect to exclusionary abuses of dominance, the report finds that such conduct can take many forms, including exclusive dealing, tying and bundling, predation, refusal to supply, and margin squeezes. In exclusionary-conduct cases, the harm is most often suffered by competitors of the infringer.

According to the report, the main harms arising from exclusionary conduct are that existing competitors may limit market presence, be prevented from competing effectively, or be forced to exit the market — while potential competitors may be prevented from entering the market. In addition, buyers in the market may be harmed by higher prices, reduced choice and/or reduced quality. The report recognizes that the main harm arising from these cases are actual economic losses (*damnum emergens*) and lost profits (*lucrum cessans*).²⁰ It summarizes the basic economic framework for calculating such damages as the difference between the factual and counterfactual profit of the company.²¹

A national court is excluded from not awarding any damages simply because the claimant cannot prove with sufficient precision the amount of harm suffered.

As to which parties may be harmed by breaches of competition law, the report describes a number of them through the supply chain. For example, it identifies:

- Direct purchasers, which are customers that purchase goods or services directly from the infringers.
- Indirect purchasers, which purchase goods or services from a supplier that is downstream from the infringer;
- End-users, which can be either direct or indirect purchasers;
- Potential customers, which are customers that would have purchased goods in the absence of the infringement;
- Competitors, which compete with the infringers directly;
- Suppliers to the infringing parties.
- Firms in connected markets (*e.g.*, suppliers of complementary goods).

The final part of section 2 discusses the conceptual framework in analyzing the calculation of the final value of damages. This generally requires the results of the counterfactual analysis to be input into a financial evaluation model.

The report describes this calculation as involving two main steps: summation of the losses from the various types of harmed claimed, and summation and movement of losses over time, including uprating and/or discounting cash flows to take account of the time value of money for infringements that lasted many years. This section concludes with a summary of the relevant variables for quantifying both damages from cartels and exclusionary conduct, depending on which type of claimant is bringing the case.

SECTION 3: METHODS AND MODELS FOR QUANTIFYING DAMAGES

Section 3 comprises the bulk of the report, as it identifies and discusses the various methods and models that can be used to quantify antitrust damages. The report suggests that the aim of any method or model designed to quantify antitrust damages is to produce a calculation of the counterfactual, or “but for” scenario (*i.e.*, what the world would have looked like without the infringement) and to assess the harm suffered by the victim of the infringement.

The report classifies the methods and models for quantifying damages into three broad groups:

- Comparator-based.
- Financial-performance-based.
- Market structure-based.²²

According to the report, in principle each approach can be used for quantifying damages for any type of antitrust infringement, and they often complement each other.

COMPARATOR-BASED METHODS AND MODELS

The comparator-based approach uses information from actual transactions in markets where there is no infringement to form the basis of the counterfactual scenario. The report identifies three ways this can be accomplished.

The first is by “cross sectional” comparison, which offers comparisons across different geographic or product markets. This approach is often referred to as the “benchmark” or “yardstick” approach.

The second is by time-series comparison, which analyze prices before, during and after the infringement. These have the advantage of including like firms or markets since they refer to the same firms and markets in both the factual and counterfactual cases.

The third is by combining the two approaches to form “difference-in-difference” models, which, for example, analyze the price for a cartelized market over time and compare that result against the change in price in a non-cartelized market over the same period. This method is aimed at avoiding the shortcoming of the other two methods in that they assume that any unexplained difference between the factual and counterfactual is due solely to the infringement.

According to the report, the comparator-based methods or models where the counterfactual is based on comparable product and/or geographic markets can vary in their degrees of sophistication. For example, a simpler technique is a comparison of averages, where the average price in an unaffected, comparable group is used as an estimate the counterfactual price.

Another simple method described in the report is interpolation, which builds on a comparison of averages in that the pre- and post-infringement period prices are used to estimate the counterfactual price.

More complex methods identified in the report are regressions, which are statistical methods used to explain the variation of a variable such a price with a number of other factors. Regression techniques address one of the main shortcomings of a simple comparison of averages (*i.e.*, finding markets that are sufficiently similar by controlling for differences in market or firm characteristics in the relevant and comparable markets). According to the report, this generally leads to more robust results.

FINANCIAL-PERFORMANCE-BASED METHODS AND MODELS

The financial-performance-based models identified in the report use financial information on comparable firms and industries, benchmarks for rates of return, and cost information from defendants and claimants to estimate the counterfactual scenario. There are two types of approaches that use financial information: those that examine financial performance and those that apply financial tools.

The former approach includes, among other things, assessing the profitability of defendants and/or claimants and comparing this against a benchmark. The latter includes the use of more general financial tools, such as discounting and multiples.

The report describes several ways in which financial analysis can be used in the counterfactual stage of a damages estimation. One way is to measure the deterioration in the financial performance of the victims as a result of the infringement. The improvement in the financial performance of the defendant also can be used a measure of the benefits derived from the infringement. Third, profitability analyses and valuations and event studies on share prices can be used to estimate harm caused by an infringement. Finally, the counterfactual price can be calculated by assessing the cost of production of the infringing parties, and combining this with information on counterfactual margins.

The report suggests there are advantages and disadvantages to employing financial-analysis-based methods. One advantage is the greater likelihood of available financial data because of corporate disclosure rules. A disadvantage recognized in the report is that it may be difficult to distinguish the impact of external factors from the impact of the infringement on financial performance.

MARKET-STRUCTURE-BASED METHODS AND MODELS

The market-structure-based models, based on “industrial organization” theory, use a combination of theoretical models, assumptions and empirical estimation to arrive at an assessment of the counterfactual scenario. According to the report, this approach involves identifying models that best fit the relevant market and using them to provide insight into how competition works in the affected market and to estimate the counterfactual price.

The report recognizes that the use of IO models in damages calculations can range from the theoretical — where models are used to provide information on certain market dynamics conceptually, to the empirical — where models are populated with data for the actual market in question in order to then estimate counterfactual values.

The report discusses in some detail the most common IO models:

- Perfect competition
- Monopolistic competition
- Bertrand oligopoly with homogeneous goods
- Bertrand oligopoly with differentiated goods
- Cournot oligopoly
- Monopoly

The choice of the appropriate model is important when the IO-based approach is used, and the report identifies certain factors that may help inform the most appropriate choice, including how prices are formed, whether the relevant product is homogeneous or differentiated, the number of firms in the market, barriers to entry, and cost structure.

The report describes two principal ways of using IO models in quantifying antitrust damages. The first is the “one model” approach, which uses an IO model to estimate the counterfactual, using the factual outcomes as inputs. This model has been applied to determine whether firm behavior is more consistent with collusion than competition.

The other is the “two model” approach, in which IO models are adopted for both the factual and counterfactual scenarios. According to the report, an advantage this approach has over the one-model is that it is typically less demanding in terms of the amount of data required.

The report cautions that the resulting damages estimates using the aforementioned IO models will be influenced to a large extent by the choice of the counterfactual model; Thus, any results should be tested. In particular, the report suggests that the more competitive the model adopted for the counterfactual, the greater the difference between the factual and counterfactual prices.

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The report describes several ways in which financial analysis can be used in the counterfactual stage of a damages estimation.

SECTION 4: FURTHER INSIGHTS FROM ECONOMICS AND FINANCE LITERATURE TO AID THE USE OF METHODS AND MODELS

In addition to the conceptual framework and the classification of methods and models, the report also discusses further insights provided by economics and finance literature that may assist in calculating a damages estimate. The report suggests that these aids can serve as general background information, a cross-check of the damages calculation, or early insight into the likely nature of the damage prior to the use of methods and models. In addition, the insights in this section can be used to facilitate the calculation of antitrust damages when there is insufficient data to apply methods and models.

For example, the report identifies several empirical studies on cartel overcharges. These studies indicate that the majority of cartels have a positive overcharge. Indeed, the report examines two recent cases in Germany that discuss whether it is appropriate to assume a cartel overcharge is appropriate. In addition, economic literature provides orders of the magnitude of overcharges of past cartels.²³

Section 4 organizes the insights by the stages of the conceptual framework of an antitrust damages claim set out in Section 2. For example, insights from economic theory and empirics are presented in some detail for the various types of harm from antitrust infringements, including the magnitude of overcharges, the lost-volume effect, which profit margin to use when deploying modeling techniques, pass-on of overcharges, interest and tax rates for discounting, using market prices to approximate firm-specific prices, and using yield to approximate price in order to fill in gaps in data series. This section is a useful tool to expand the available resources when calculating antitrust damages.

SECTION 5: ARRIVING AT A FINAL DAMAGES VALUE

The report does not rank the methods and models that can be used to calculate damages. Not surprisingly, it recognizes that the choice of which method and/or model to use depends on the specifics of each case, primarily the availability and quality of data and information, and the basis of the counterfactual used in a particular model. In short, the more data that is available, the greater the range of methods and models that can be used. In addition, the report notes that the choice of model will depend on such legal rules as levels of evidence required and burden of proof.

Ultimately, it is up to the courts to decide on a specific amount of antitrust damages to be awarded. Since in any given case it is likely possible to employ more than one approach to quantify damages, a court is typically presented with multiple estimates of damages. According to the report, economics literature has identified two main solutions for arriving at a final, single damages value.

First, the court can identify one method or model that is most appropriate for the case at hand and use the output from that model as the best estimate for the harm. The report identifies two advantages to using this approach: It can provide greater clarity for the court in terms of where each party stands if both choose a single model, and it permits the court to afford greater weight to a preferable or superior modeling approach.

Second, the court can “pool” several model results and combine into a single value the results of each. For example, the report identifies that one “robust” approach is to simply take the mean average of the available damages estimates to get the best estimate of the actual harm. There are two advantages to pooling. When the models

rely on different subsets of available data, combining the forecasts means the final value reflects more of the underlying data (and hence more of the available information), and is likely to reduce biases in the individual models.

Section 5 concludes with two hypothetical examples, the first quantifying damages from a price-fixing cartel, and the second quantifying damages from exclusionary abuse. Each illustration follows the conceptual framework (Section 2) and then shows how a combination of comparator-based, financial-analysis-based and market-structure-based approaches (Section 3) can be used to quantify the damages, aided by further economic, theoretical and empirical insights (Section 4). These are helpful examples of how the concepts in the report can work in practice.

IMPLICATIONS IN THE REAL WORLD

The report will likely have real-world implications throughout the EU and beyond. As the policy initiatives discussed in the White Paper are implemented to remove or lessen obstacles for victims to bring private antitrust actions, greater attention will need to be paid to the procedures for fully compensating victims for harms suffered. The report should serve as an instructive resource for the EC and member states' national courts for expanding their knowledge and expertise in quantifying damages in antitrust actions.

In addition, it will help bring some uniformity to damages analyses and results among the courts within the EU.

The report is also a useful tool for understanding how various approaches have been employed by courts in the past. Throughout the report, there are illustrations of current practices in damages actions in courts across Europe (and the U.S.), that describe some of the different legal approaches in different jurisdictions and provide concrete case examples. The examples are related to the specific concepts presented in the report.

Finally, the report provides invaluable guidance on quantifying antitrust damages for any practicing antitrust attorney, including those outside the EU. It can act as a primer to those who are new to the concept of quantifying antitrust damages, as well as a refresher and introduction to new concepts for those already knowledgeable on the issues, particularly the section on further insights.

Overall, the report will advance the EC's primary objective to provide measures to ensure effective antitrust damages actions in the EU, particularly with respect to quantifying antitrust damages to fully compensate victims of antitrust infringements.

NOTES

- ¹ Oxera Consulting, *Quantifying Antitrust Damages: Toward Non-Binding Guidance for Courts*, Study Prepared for the European Commission (December 2009), available at http://ec.europa.eu/competition/antitrust/actionsdamages/quantification_study.pdf.
- ² COMM'N OF THE EUROPEAN COMMUNITIES, *WHITE PAPER ON DAMAGES ACTIONS FOR BREACH OF THE EC ANTITRUST RULES*, COM(2005) 165 final (Apr. 2, 2008), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0165:FIN:EN:PDF>.
- ³ COMM'N OF THE EUROPEAN COMMUNITIES, *GREEN PAPER ON DAMAGES ACTIONS FOR BREACH OF THE EC ANTITRUST RULES*, COM(2005) 675 final (Dec. 19, 2005), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2005:0672:FIN:EN:PDF>.
- ⁴ COMM'N OF THE EUROPEAN COMMUNITIES, *GREEN PAPER ON DAMAGES ACTIONS FOR BREACH OF THE EC ANTITRUST RULES*, SEC (2005) 1732; available at http://ec.europa.eu/competition/antitrust/actionsdamages/sp_en.pdf.

- ⁵ COMM'N OF THE EUROPEAN COMMUNITIES, WHITE PAPER ON DAMAGES ACTIONS FOR BREACH OF THE EC ANTITRUST RULES, SEC (2008) 404; available at <http://eurlex.europa.eu/LexUriServ/LexUriServ.do?uri=SEC:2008:0404:FIN:EN:PDF>.
- ⁶ Comm'n of the European Communities, Commission Staff Working Paper Accompanying The White Paper on Damages Actions for Breach of the EC Antitrust Rules, SEC (2008) 404 at ¶199; see also White Paper at 7.
- ⁷ White Paper at 2; see also Case C-453/99, *Courage Ltd. v. Crehan* [2001] ECR I-6297, and Joined Cases C-295/04 to C-298/04 *Manfredi and others v. Lloyd Adriatico Assicurazioni S.p.A. and others* [2006] ECR I-6619.
- ⁸ White Paper at 3.
- ⁹ *Id.*
- ¹⁰ Staff Working Paper at ¶¶187, 190 and 192.
- ¹¹ *Id.* at ¶196.
- ¹² White Paper at 7.
- ¹³ Report at 12-36.
- ¹⁴ *Id.* at 37-86.
- ¹⁵ *Id.* at 87-128.
- ¹⁶ *Id.* at 129-49.
- ¹⁷ According to the report, there have been relatively few cases of exploitive abuse of dominance found by competition authorities or the courts. To the extent they occur, the most common form is "excessive pricing." The harm caused by excessive pricing is similar to that caused by cartels, *i.e.*, higher prices.
- ¹⁸ Report, *supra* note 1, at 15.
- ¹⁹ *Id.*
- ²⁰ See Joined Cases C-295/04 to C-298/04 *Manfredi and others v. Lloyd Adriatico Assicurazioni SpA and others* [2006] ECR I-6619, at ¶¶95-97.
- ²¹ Report, *supra* note 1, at 22-23, Figures 2.2 and 2.3.
- ²² In drawing up these "new" classifications, Oxera considered previous groupings of methods and models presented in other contexts, including the EC's 2004 Ashurst study on antitrust damages, the EC's 2007 CEPS, EUR, LUISS study on the impact of policy options for damages actions, the Bundeskartellamt and U.S. antitrust case law. *Id.* at 42-3.
- ²³ The EC's directorate-general for competition hosted a program Jan. 26, 2010, for economic experts in Brussels titled "Quantification of Harm in Damages Actions for Antitrust Infringements: Workshops of Economic Experts." There were three sessions: "Harm From Price Overcharges," "Harm From Exclusionary Practices" and "Methods, Models and Techniques to Quantify Antitrust Harm." The EC website includes 18 written contributions from the experts on the issue of quantifying damages, which are useful insights for consideration. See http://ec.europa.eu/competition/antitrust/actionsdamages/economist_workshop.html.



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