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Too Much of a Good Thing?: Is Heavy Reliance on Leniency Eroding Cartel Enforcement in the United States?

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Too Much of a Good Thing?: Is Heavy Reliance on Leniency Eroding Cartel Enforcement in the United States?

Megan Dixon, Ethan Kate, & Janet McDavid[1]

I. INTRODUCTION

The United States Department of Justice Antitrust Division's leniency program has seen unparalleled success over the past two decades as one of the most effective law enforcement tools available to identify and prosecute international cartels. Leniency has been the key driver in facilitating the Division's takedown of cartels of a magnitude and longevity previously not contemplated by most in the competition field.

Twenty years into its regular use of this powerful tool, however, questions have begun to emerge about whether the Division is relying too heavily on the leniency program, to the detriment of some of its overall enforcement goals. Does dependence on leniency as the cornerstone of one's regime have unforeseen or, at least, undesirable consequences? Should leniency programs play different roles in emerging, established, and sophisticated regimes? Has the success of the leniency program become a bit of crutch? Has the Division's seeming obsession with ever-increasing statistics on the number of dollars fined or of foreign nationals jailed caused it to lose sight of some other important goals? Is it time for the Division to assess critically whether a larger percentage of its resources should be devoted to attempting to detect and prosecute violations that come to its attention via other avenues such as targeted community outreach and econometric market analysis?

Answers to these questions may depend, to some extent, on what you believe makes a cartel enforcement program successful. It seems fair to say that the Antitrust Division has taken the position that Big Is Good. And we wholeheartedly agree that it is in large part the shocking size—in every respect—of some of the cartels prosecuted as a result of the leniency program that have made the U.S. enforcers world leaders in competition policy, and that significantly changed the face of global cartel enforcement just as the "global economy" became a reality.

It is hardly surprising that combining an extremely successful and highly visible program with dwindling resources has led the division to rely heavily on the leniency program over the past couple of decades, and thus its focus on massive international cartels brought in through the leniency program has also made sense. That focus brought significant attention to the harms caused by cartels, thereby propelling cartel enforcement into a previously unknown world spotlight. And, unquestionably, in a gross economic sense blockbuster cartels do more harm than smaller, domestic cartels do.

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But we are not convinced that at this point in the U.S. regime's development, the Division should continue to focus the vast majority of its resources on these blockbuster cartels. We are not unaware of, or unsympathetic to, the severe resource constraints the Division currently faces, nor do we suggest that the Division has not pursued and had impressive success outside the leniency-generated blockbuster cartel space. We are simply suggesting that it may be time to take a fresh look and potentially reallocate some scarce resources to other components of the U.S. competition enforcement program.

II. THE RISE OF THE LENIENCY MODEL

According to the Antitrust Division's own statistics, 20 years ago more than 90 percent of the Division's cases were generated through old-fashioned investigation techniques like community outreach; customer, competitor, or employee complaints; economic analysis of markets, bidding, or pricing patterns (often referred to as "screens"); or other forms of proactive investigation. And although the Division has had a leniency program since 1978, prior to the mid-90's it was, according to former Deputy Assistant Attorney General Scott Hammond, "rarely utilized," and responsible for zero detections of an international or even a large domestic cartel.[2]

What changed in the early to mid-90s? The Division overhauled its leniency policy, making it more accessible and increasing incentives for companies considering self-reporting. Between then and now, the 90/10 numbers have flipped completely, and then some. Again according to Hammond, by 2010 the leniency program was responsible for more than 90 percent of the criminal fines imposed in antitrust cases.[3]

Key components of the Division's modern leniency program are the "Amnesty Plus" and "Penalty Plus" provisions. Amnesty Plus applies when a company implicated in a cartel investigation discloses previously undetected antitrust offenses involving a different cartel. This disclosure affords the company significant benefits as to its penalty in the first offense, and amnesty as to the second. Amnesty Plus induces companies to clean house, and for those who fail to do so, there is Penalty Plus, under which the Division may recommend sentences above the Sentencing Guidelines range for those same offenses. Amnesty Plus is responsible for at least half of the Division's cases over the past decade.

The Division has created other incentives for potential leniency applicants as well. In 1996, a Memorandum of Understanding ("MoU") between the DOJ and immigration authorities was implemented that makes Sherman Act violations "crimes of moral turpitude" and thereby subjects foreign nationals convicted of antitrust crimes to a 15-year ban from the United States. But the MoU provides for a waiver of the ban for individuals who forego jurisdictional arguments and come to the United States voluntarily and plead guilty. This naturally creates a strong incentive to cooperate for individuals who want, or need, for their employment to continue to travel to the United States. And because the ban does apply to individuals who voluntarily come to the United States to stand trial, some have argued that this agreement

[2] Scott D. Hammond, Deputy Assistant Att'y Gen., Antitrust Div., U.S. Dep't of Justice, *The Evolution of Criminal Antitrust Enforcement Over the Last Two Decades*, Remarks Presented at the 24th Annual National Institute on White Collar Crime 2 (Feb. 25, 2010), *available at* http://www.justice.gov/atr/public/speeches/255515.htm.

[3] *Id.* at 3.

unfairly pressures foreign defendants to plead guilty rather than exercise their right to challenge the Division's evidence at trial.

In 2004, the Division won another victory on the leniency front with the passing of the Antitrust Criminal Penalty Enhancement and Reform Act ("ACPERA"), which was intended to increase the criminal penalties for antitrust violations as well as the incentives for participating in the leniency program. Under ACPERA, maximum fines for corporations increased from $10 million to $100 million, while fines for individuals increased from $350 thousand to $1 million. Additionally, maximum prison sentences for individuals were increased from three to ten years.

ACPERA also further incentivized leniency applicants by reducing potential damages owed to civil claimants and eliminating both treble damages and joint and several liability for successful applicants. Extended for an additional ten years in 2010, ACPERA now also includes a "timeliness" requirement for leniency applicants to assist civil claimants.

III. DOWNSIZING THE DIVISION

While it could fairly be argued that the Division has always been under-resourced relative to the value it creates and the importance of its mission in a free market economy, its resources problem has only become more acute in the past few years, despite its investigations increasing in both frequency and scale. Post-2008 budgets have shrunk, Division employees have been furloughed, and hiring has been frozen. And after the Division closed four field offices in January 2013, its cartel enforcement team was slimmed down by more than 30 percent.

IV. EMERGING CRITIQUE

There is widespread agreement that an effective competition enforcement program should both detect and deter cartel behavior. The principal criticism of leniency as the most heavily relied upon tool in such a program is that its detection component is almost purely reactive, and, standing alone, its deterrent potential may be lower than many forms of proactive investigation, such as market monitoring and outreach and training programs.

The Division has long held, a "prerequisite to building an effective amnesty program is instilling a genuine fear of detection."[4] True. But some would argue that a regime wherein cartelists may fear being exposed by their co-conspirators in exchange for leniency, but where they face no real danger of otherwise being detected, is lopsided and thus less effective both as a detector of and a deterrent to bad behavior than if resources were more evenly allocated between deterrence and detection.

The reactive approach to enforcement exemplified by a very heavy reliance on leniency and a bias toward blockbuster cartels may be leaving a wide gap where cartel behavior is likely to continue unabated by those who review the statistics and decide they are at low risk of detection. This may be especially true as to smaller or domestic cartels. If cartel enforcement is simply all about huge numbers, perhaps this is acceptable. But in these difficult economic times, those smaller cartels—while undisputedly having a lesser impact on the global economy—may have

[4] Scott D. Hammond, Director of Criminal Enforcement, Antitrust Div., U.S. Dep't of Justice, *Cornerstones of an Effective Leniency Program*, presented before the ICN Workshop on Leniency Programs (Nov. 22-23, 2004), *available at* http://www.justice.gov/atr/public/speeches/206611.pdf.

more harmful direct effects on their victims. Take as an example a comparison between the following: a global automobile cartel fixes the price of a part that increases the cost of every car sold over a 5-year period by ten dollars. Let's say for simplicity there are 100 million cars sold during the period. That's a lot of cumulative overcharge! But does paying $10 more for a car have much effect on the individual victims, who would likely purchase only one car in that period? Probably not.

Take, on the other hand, a domestic dairy products cartel wherein the cartelists agree to increase the prices of milk, yogurt, ice cream, and cheese by 40 percent at all military PXs in the western United States. Regardless of how much those military families in Idaho and Colorado may like cheddar, undoubtedly the volume of commerce—and the effect on the global economy—would be exponentially lower. But the effect on those military families is likely to be significantly more acutely felt than would be paying $10 more for a new car every five years.

Even participants in a blockbuster cartel may decide that they are unlikely to be detected because, for example, their cartel is so profitable that none of the conspirators is likely to self-report. In a leniency-dependent system, this cartel may not surface until it becomes less profitable and falls apart, such that many of the cartels that are "detected" in this fashion may actually be old news.

A focus on historic cartels also poses a risk that the Division will be too late to prosecute culpable parties. Following the Second Circuit's recent decision in *Grimm*,[5] courts may require very specific kinds of overt acts in furtherance of a conspiracy to toll the statute of limitations. Payments received merely as a result of a conspiracy may be insufficient to extend the duration of the conspiracy for statute of limitations purposes. In a reactive regime, participants may be unlikely to come forward—even where a previously successful cartel is no longer profitable—when they can instead wait it out for the statute of limitations to pass, thereby avoiding a costly investigation related to a leniency application. While the Division has worked to incentivize leniency applications, *Grimm* may at least give prospective applicants pause before coming forward.

Overreliance on leniency also has the potential to seriously over-punish those who operate in an industry that is currently on the Antitrust Division's "hot list," especially where many of the conspirators are incentivized by Amnesty Plus to continue to try to offer more and more information on other alleged cartels to curry favor with the Division and collect cooperation credit, and perhaps also to harm their competitors in the process. Not infrequently, much of the "additional" conduct that is offered up, even if technically a violation, is fairly old, fairly marginal, has weak evidence, or has some combination of those problems. Should the Division be spending its scarce resources on those kinds of cases? We would argue no, but the current leniency-dependent model encourages this result.

In Congressional hearings held in November and December 2013, the United States Senate Subcommittee on Antitrust, Competition Policy and Consumer Rights questioned whether the Division has become overly reliant on its leniency program to generate cases. In particular, the Senators expressed concern as to whether the leniency program and the big dollar,

[5] *United States v. Grimm*, No. 12-4310 (2d Cir. 2013).

low-hanging fruit cases have been unfairly diverting attention from other enforcement tools and goals, leaving the smaller, less sexy cases unaddressed.

In January of this year, Frédéric Jenny, the chairman of the OECD's Competition Law and Policy Committee, and a judge at the Supreme Court of France, stated that there is no evidence that increased enforcement or more leniency applications have decreased cartel behavior. Jenny acknowledged that more enforcement has resulted in a larger number of cartels being detected, but noted that some of the latest investigations concern recently active cartels, which he believes shows that the methods competition authorities have been employing to detect and prosecute are not effectively deterring cartel behavior.

In support of his conclusion, Jenny and others[6] have pointed to the investigations into LIBOR, Euribor, and auto parts, all of which are recent, massive, and widespread cartels, but which were identified through self-reporting by leniency applicants—not through enforcers' independent investigative efforts. Jenny concluded that given their size and reach, and the fact that industry analysts had questioned the operation of some of these markets long before the investigations began, it was "quite extraordinary that the[se cartels] went unnoticed, which probably shows that the screening of markets is not sufficiently used."[7]

V. CONCLUSION

The Antitrust Division's leniency program is by all accounts a model for others around the world. It has served the Division supremely well in its cartel-cracking mission for twenty years. But too much of this good thing may be bad for the Division's long-term health. Over-reliance on leniency to prevent and detect arrangements that are axiomatically tight knit and secret is particularly dangerous because it relies on characteristics that are anathema to the wrongdoing that it seeks to address.

Cartels may be among the least obvious examples of conduct likely to be deterred solely by relying on someone coming clean in the hope of leniency, which is why enforcers also need to be out there actively employing other tools to look for violations at the same time. Therefore, the Division should be mindful that relying too heavily on leniency may be detrimental to its overall goal of decreasing harmful cartel activity in the United States and across the globe. Thoughtful consideration of the program in light of the current global economic situation and the Division's own enforcement goals may suggest that some reallocation of resources and/or careful prioritization of pursuits is warranted.

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[6] *See*, e.g., Rosa M. Abrantes-Metz & D. Daniel Sokol, *The Lessons from LIBOR for Detection and Deterrence of Cartel Wrongdoing*, 3 HARV. BUS. L. REV. 10 (2012).

[7] *See Cartel activity worldwide has not dropped despite harsher enforcement – OECD Competition Committee chairman*, 6 January 2014, Policy and Regulatory Report.

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10 Ways to Preserve the Lustre of Leniency

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10 Ways to Preserve the Lustre of Leniency

Grant Murray & Douglas Tween[1]

I. INTRODUCTION

Today, the allure of antitrust immunity is unmistakable. Almost all of the most prominent global cartel cases have originated from immunity applications and, in recognition, new leniency regimes are being adopted or fine-tuned in all key antitrust regimes around the world. But there is a risk that a combination of shrinking resources devoted to enforcement, and a lack of transparency and convergence in existing leniency regimes, could lead to a decline in the efficiency of leniency regimes. In this article we suggest 10 steps that will prevent any decline from occurring.

The effectiveness of leniency regimes in unearthing serious antitrust violations is apparent in the European Union, where contemporary anticartel enforcement by the European Commission has been characterized by a sharp drop in own-initiative cases. In fact, since Commissioner Almunia's tenure began in 2010, only one of the 20 cartel decisions adopted by the Commission is thought to have been an own-initiative case. Almunia's predecessor, Commissioner Kroes, seemed to attach a high value to own-initiative cases—regularly taking the opportunity to emphasize the frequency and success of cases that the Commission had started itself—reminding the business community that cartels are weaker than their weakest member.

Of course, Almunia's apparent reliance on the EU immunity program may reflect nothing more than an inherited workload. But the Commissioner is known to be a pragmatic enforcer who places a high value on other enforcement tools, such as the cartel settlement and commitments procedures.

The allure of leniency is, of course, directly related to the likelihood that infringing conduct is detected and punished harshly in a particular jurisdiction. The startling financial penalties that were avoided by banks in the recent EU financial benchmark cases make it difficult to argue that leniency is anything but a very good option. In the *Yen Interest Rate Derivatives* cartel the EU immunity applicant escaped a fine of EUR 2.5 billion—which would have been the highest fine ever to have been imposed on a company by the Commission (and in fact almost twice the value of all fines imposed by the Commission in 2013). So leniency can have a very high value. (As trustbuster Teddy Roosevelt famously said, "Speak softly, and carry a big stick.")

The picture is, of course similar in the United States, where antitrust amnesty first began. The Department of Justice Antitrust Division ("DOJ") is rightly proud of its Amnesty Program, describing it as "...by far the most effective tool for detecting cartel activity." In fact, in the years 2004 to 2010, around three quarters of all criminal cartel cases filed by the U.S. Antitrust Division

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are thought to have been initiated or advanced by information received from a leniency applicant. The ability to escape a likely custodial sentence (no matter the nationality of the defendant) has no doubt been a significant factor. Amnesty Plus (where a company under investigation self-reports another cartel and receives immunity in relation to the "new" cartel, as well as a reduction in relation to the existing one under investigation) has also become "…an increasingly important cartel-detection and case-generation tool."[2]

Against that backdrop, it is no surprise that the U.S. amnesty regime has inspired and been replicated by leniency programs in myriad countries. New countries come on line (Taiwan) and more established antitrust enforcers (Canada, United Kingdom) update and fine-tune their programs—just as the United States and the European Union have done in the past. Indeed, the United States is currently amending its ACPERA rules to give even greater protection to whistle-blowers. Amnesty Plus has also been copied elsewhere (United Kingdom, Singapore).

But high fines and/or individual sanctions do not guarantee leniency applications. Leniency regimes will only be effective if there is transparency in terms of agency procedures and trust between the agency and a potential applicant. If those elements are missing then high fines may disincentivize immunity applications completely. There are still some antitrust regimes out there that have high fines but no workable leniency program. As the ICN has said, the key elements of an effective leniency program are significant sanctions, a high risk of detection, and transparency and certainty.

Even in jurisdictions where leniency regularly leads to cartel investigations, observers may question the actual value of leniency—theorizing that leniency applications are typically made towards (if not after) the end of the cartel's natural life. Recent high profile cartel cases (in financial services and the automotive sector) are somewhat of a paradox: the cascade of cartel cases shows the effectiveness of leniency (and Amnesty Plus) but also suggest that cartel conduct took place in countries that were known at the time for their strict approach to cartel enforcement.

II. COULD LENIENCY LOSE ITS LUSTRE?

No one would deny the very obvious financial benefits of leniency. But at the same time there seems to be an unremitting flow of cartel cases. Does this bring into question the effectiveness of leniency programs as a means of cartel prevention? Are legal and practical considerations beginning to de-value leniency? It is certainly the case that more antitrust agencies are imposing fines in respect of the same cartels and looking to criminalize cartel conduct. National rules against double jeopardy may not help. In addition, private damages actions—once the preserve of the United States—are now common in other regions (notably in certain EU Member States) and legislative proposals seek to make it easier for victims of cartel conduct to be compensated.

Will the cutting of enforcement resources due to financial pressures globally lead to less own-initiative investigations and less vigorous enforcement which, in turn, decreases the risk of

[2] http://search.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP(2012)25&docLanguage=En.

getting caught, which decreases the incentive to apply for leniency? The United States has cut the number of cartel enforcers by more than one third due to budget reasons over the last two years.

In the European Union the Commission enforced against all of the air cargo airlines that applied for leniency and confessed—and none of those that did not. In the U.S. air cargo cartel, the DOJ imposed high sanctions on the airlines that came in early and gave minimal sentences to those that held out for several years. Is there a risk that agencies will one day lack resources to pursue investigations as thoroughly as they would like? A lack of resources could one day lead to a tipping point where it is preferable for investigated companies to either obtain immunity or to contest matters for as long as possible, rather than be second-in—because the enforcers do not themselves have the resources to conduct a full investigation.

The incentive to self-report may be strong now but even the more experienced antitrust agencies need to keep their programs under review to ensure the ongoing effectiveness of their regimes. Here are 10 ways to keep leniency regimes working

#1. Enact clear rules and explain how discretion is exercised: To build trust, companies need to understand the process. Transparency and guidelines are important even in respect of areas where discretion will be used. The need for clear guidance on the leniency prize is evident in light of a recent trend in the European Union. In *Wire Harnesses*, the Commission categorized specific violations as separate cartels, such as particular rigged bids, rather than attempting to show an industry-wide cartel. This means that a leniency applicant that believes it is "second in" for the overall case could receive a lower discount than anticipated because it is not "second in" for all the infringements. Lack of predictability about how an agency will approach evidence supplied in good faith could deter leniency applications from being made, especially given the diminishing returns of being second or third in.

#2. Align the key tenets of global leniency regimes: Cartels often have an impact in multiple countries. There may not be leniency protection in all those countries and, even in countries where there is active enforcement and a leniency regime, the company may not be first in—perhaps because the conditions for granting leniency were unclear. There may also be "copy cat" investigations where an agency opens an investigation at a time when the initial investigation in the "key" jurisdictions has already been completed (and the fines imposed/harm ended). So even companies that wish to draw a line under their conduct cannot manage exposure everywhere. Even within the European Union, there is no-one-stop for immunity, just model short-form applications.

Some alignment of the key tenets of leniency regimes would help. For example, agencies approach markers very differently with different requirements regarding duration, scope, information, etc.[3] This creates a conflict for obtaining the marker and then perfecting it, and therefore adds uncertainty that can operate as a disincentive. It may cause a problem in the early phases when an applicant is investigating potentially affected products and markets. Companies may also hesitate to apply for a narrow marker until they have secured a broad marker in another

[3] A "marker" is the confirmation given to an immunity applicant (company or individual) that he/she/it is the first party to request a grant of immunity with respect to a particular cartel and meets the relevant conditions.

jurisdiction. This could deter the company from applying at all as the broad marker may also expose the company in other countries.

International consensus on the notion of "nexus" between a cartel and a particular country would help avoid "gaming" of the system (where a rival is first-in, prompted by another company's leniency application) and reduce risk of "copy cat" investigations years later. Alignment between leniency programs would also improve the quality of leniency applications received by agencies.

#3. Create one-stop-shop for leniency: A genuinely innovative way to address the problems caused by the geographic cascade of cartel investigations would be to develop a mechanism to assist a company (which has decided to self-report) to receive appropriate and consistent benefits internationally. One proposal along these lines has been the creation of a global "one-stop shop" whereby applicants would apply for leniency markers through an international clearinghouse of sorts. Each participating jurisdiction would then apply its own policies and procedures to determine whether the applicant has successfully perfected its marker.[4]

#4. Make sure that a valuable second prize is available: Many leniency regimes around the world provide the possibility of complete immunity for the first company to self-report a violation. And while many also provide an incentive for the second and subsequent applicants, whether as a formal part of the leniency program or in practice as part of settlement arrangements, not all of even the major antitrust jurisdictions do (e.g. Brazil, South Africa). Leniency for subsequent applicants has a number of obvious advantages for the agency:[5]

- The second applicant's evidence may corroborate—or bring into question—the evidence already received from the immunity applicant. The evidence provided by a subsequent applicant therefore provides an essential check on the veracity of evidence provided by a company which may not be aware of the full facts—or might have misrepresented its own involvement and the operation of the alleged cartel in order to increase the chances of obtaining immunity; for example, by omitting evidence of coercion.
- The possibility of an incentive for subsequent applicants could provide for a smoother and quicker investigation of cases since an applicant obtaining immunity in one country, but a reduction for being in second place in another, is more likely to provide a waiver for the exchange of confidential information between those countries.
- Leniency for subsequent applicants can bring in more cases: an incentive to launch internal investigations may increase the likelihood of "Amnesty Plus" type leniency applications.

The availability of leniency for subsequent applicants can also address some of the drawbacks described above which result from the proliferation of global cartel investigations.

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[4] John Taladay, *Time for a Global "One-Stop Shop" for Leniency Markers*, ANTITRUST (Fall 2012).

[5] These arguments are more fully developed in the submission of BIAC to the 2012 OECD Policy Roundtable on Leniency for Subsequent Applicants http://www.oecd.org/competition/Leniencyforsubsequentapplicants2012.pdf.

The very existence of a potential reward for subsequent applicants can strengthen the incentive for a company to apply for leniency in the first place since companies that are concerned about whether or not they would be first-in (especially in countries that do not provide a marker or reliable information about a prospective applicant's place "in the queue") may nevertheless apply for leniency in the knowledge that they stand a good chance of obtaining a reduction even if they are not the first to apply.

#5. Adopt global guidelines to avoid double counting: Assuming there is a reduction for second or third applicants, companies will still look very carefully at the likely size of the fine. Naturally the reward for being second- or third-in has to be materially less than that available for being first-in. However, the cumulative approach to fines across the world may one day be enough to deter a company from coming forward. The narrow scope of the rule against double jeopardy (and the absence of any provision of international law to ensure overall optimal deterrence) means that countries can each fine companies in respect of the same cartel for the harm caused in their respective countries.

However, some steps could be taken to preserve the leniency incentive. In particular, some alignment as to the type of sales taken into consideration when setting fines would be sensible in order to eliminate double counting. This approach need not be confined to subsequent applicants. The European Commission and DOJ have been sensitive to the issue of double counting in respect of global cartels (even though they do not have to do this). The same is true in relation to custodial sentences (*Marine Hoses*). A large obstacle may be the political and financial implications of "ceding" jurisdiction and allowing another agency to impose fines.

#6. Ensure that criminal immunity can be offered: There is a clear trend towards imposing personal sanctions on individuals when setting a corporate fine. In order to preserve the leniency incentive, corporate immunity must also give rise to criminal immunity for cooperating employees. That is the case in many countries such as United States and United Kingdom, but not everywhere. In Australia it is the CDPP that makes the decision on whether to grant criminal immunity to the company and its employees even if the ACCC is willing to offer conditional civil immunity.

Failure to automatically extend the benefits of immunity to individuals may deter companies from applying because they are unable to secure the cooperation of a key individual. Lack of automatic criminal immunity in a jurisdiction could also mean that an implicated individual does not bring the violation to light (because of the exposure it means for that individual) or applies for immunity himself (precluding the company from being first). Each of these factors muddies the waters for a would-be immunity applicant—even where the company has discovered a rogue employee and wants to cooperate fully itself. These issues can also arise in a jurisdiction where criminal immunity is available but where the individual is concerned they will be exposed in other countries.

#7. Immunize a successful applicant for all related criminal offenses*:* These days a great many antitrust cartels also infringe other criminal laws, e.g. wire fraud, Foreign Corrupt Practices Act ("FCPA") in the United States. It is unrealistic to proceed as if an antitrust infringement exists in a vacuum. An agency's offer of antitrust immunity is illusory if the individual could be prosecuted for other related crimes.

There is a strong case to be made for immunity in respect of FCPA when antitrust immunity is sought. Technically, there may be no issue of double jeopardy but the additional offense is really just part of the former—and the two infringements give rise to the same effects. This issue is arising in the financial services sector. Companies are perhaps fined by regulators first as they are in constant dialogue with them. Could this be another area (as in relation to fines and individual sanctions) where agency discretion could be exercised to impose one fine at the right level?

#8. Manage the tension with private actions: There can be a tension between encouraging leniency applicants to report all details of their infringements and the right of cartel victims to claim damages in court. In particular, leniency applications may result in more interesting or easier discovery/disclosure for claimants (especially if it is possible to obtain the actual incriminating leniency application—which, of course, is evidence that would not otherwise exist). The tension becomes even greater when applicants feel the need to make broad applications to cover the full range of products that they believe may have been cartelized. In the United States, the de-trebling of damages and the elimination of joint and several liability goes some way to addressing the tension (which may be less anyway given the attractions of criminal immunity).[6]

Further, in countries where the infringement decision is not binding as to liability (e.g. the United States and many other countries outside the European Union), leniency has the disadvantage that it makes it practically impossible to contest liability whereas non-leniency applicants might continue to do so even after an infringement decision (e.g. as to duration, particular products involved, etc.).

In the European Union a common question is whether exposure to damages will prevent companies from applying for immunity. However, this does not appear to be the case. Exposure may mean that companies are careful about the scope of the final decision—e.g. settle a cartel case to avoid a full decision and even appeal (despite being the immunity applicant) to ensure that the affected products etc. are not described in overly wide terms in the final infringement decision. However, this may change as EU private actions are on the increase and class actions may one day be the norm.

The European Commission has published a draft Directive that tries to strike the right balance between leniency and private actions. Perhaps the thorniest issue is access to leniency evidence. The EU Leniency Notice states that, under normal conditions, public disclosure of documents and written or recorded statements received in respect of the Leniency Notice would undermine certain public or private interests. However, in *Pfleiderer*, the ECJ held that EU law must not be interpreted as precluding a person who has been adversely affected by an infringement of EU competition law from being granted access to documents relating to a

[6] Note, however, that the de-trebling is not automatic. In *In Re: Aftermarket Automotive Lighting Products Antitrust Litigation* the court ruled that the whistle-blower was not entitled to limitation on civil damages because it had failed to provide satisfactory cooperation. The court held that the applicant should have disclosed a statement from an employee even though the statement had not been confirmed as accurate. This ruling is the first time a court has denied a leniency applicant ACPERA's single-damages protection for failure to provide sufficient cooperation and underlines the extent of the cooperation obligation.

leniency procedure. The ECJ invited national courts to balance the conflicting aims thereby giving rise to an inconsistent and unsatisfactory approach in the protection of leniency evidence.

No doubt because it is difficult to weigh conflicting and very different interests the European Commission has since published a draft Directive which sets out new rules relating to the disclosure of evidence. There are three categories: (i) evidence that deserves total protection (leniency statements and settlement submissions); (ii) documents that were prepared during proceedings (which can be disclosed once the agency has taken a decision the case) and (iii) pre-existing evidence for which there is no protection. The Commission is therefore trying to give some protection and transparency to both parties.

Another key plank of the Directive is to manage the financial exposure of an immunity applicant. Currently, cartelists are jointly and severally liable for damages. The draft Directive proposes to limit the liability in damages of a successful immunity applicant to that owed to its direct or indirect customers (except when the claimants can show that these are unable to obtain full compensation from other cartelists). The aim is to ensure that immunity applicants still come forward without limiting the right to full compensation.

The draft Directive also extends the limitation period for claimants and sets forth a presumption of harm. Overall, the Commission is trying to manage the tension between private damages and an effective leniency policy. It remains to be seen whether these extra elements will tip too far in the interest of the claimants meaning that immunity applications become riskier. That tension will be far greater as and when class actions are possible in the European Union.

#9. Adopt realistic but sympathetic cooperation obligations: There is a risk of harming leniency incentives when the cooperation requirement is unclear, unrealistic, or conflicts with requirements elsewhere. For example, the agency will legitimately require access to employees and perhaps even former employees—but leniency should not be lost if the company has acted in good faith to secure cooperation but still fails to do so. Guidance needs to make it clear that the agency only expects the company to do its best, giving reasonable examples of what would not be acceptable.

Agencies of course need to be aware that a company may be looking to make a number of applications. The U.K.'s OFT at one stage implied that companies may not be cooperating if they conducted too full an investigation (which they obviously have to do to understand their liability and obtain a marker in countries where more information is required than for an OFT marker). A similar issue arose in relation to legal professional privileges. At one stage the OFT wanted to make early interview notes disclosable. This was intended to assist the OFT but raised a number of controversial issues including concerns about whether the disclosure would mean that the notes could be used in other jurisdictions.

#10. Remember that "You get what you pay for:" Are there problems inherent in rewarding the very offender that should be punished? Is there a risk that the enormity of worldwide exposure leads the applicant to exaggerate their involvement—or even characterize a mostly vertical arrangement as a horizontal one in order to bring it within the class of agreements for which leniency is available in a given country? In some countries an individual whistle-blower can be rewarded (United Kingdom, South Korea). There is an open question as to whether this leads to frivolous claims or whether it actually fills a gap. Certainly the South

Korean model seems to work well (and the equivalent in the tax sector in the U.S. False Claims Act works very well). However, there is no known case of it being used to success in the United Kingdom and the DOJ has not adopted it.

III. CONCLUSION

Successful regimes engender trust by being clear and transparent—explaining how discretion will be applied and being sensitive to the needs of the applicant (including in relation to other jurisdictions).

But the lesson from history is that leniency regimes need to be updated to keep them working as markets and business activities change.[7] Global cartels, the proliferation of agencies, subsequent "copy cat" investigations, and class actions may one day deter companies from applying for leniency (or at least in certain cases).

Work at the global level is needed to align the key tenets of a leniency regime (like the ICN Recommended Practices for pre-merger control). This would bring greater predictability for companies who wish to put their houses in order. Agencies should also eliminate double counting when imposing fines. A one-stop shop would be even better to ensure optimal use of leniency and high quality applications.

Agencies may be reluctant to make changes to a system that they see as working well (at that point in time). But shortcomings in even the best leniency regime (e.g. poor or unpredictable benefits for subsequent leniency applicants) will be magnified by the inevitable growth in class actions and exponentially increasing fines. The stakes may change. Agencies need to keep their rules and procedures under review to ensure that leniency does not lose its lustre.

[7] For example, the European Union amended its leniency program to provide greater up-front certainty for applicants and the U.S. introduced Amnesty Plus.

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The “Discoverability” of Leniency Documents and the Proposed Directive on Damages Actions for Antitrust Infringements

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The "Discoverability" of Leniency Documents and the Proposed Directive on Damages Actions for Antitrust Infringements

Kristina Nordlander & Marc Abenhaïm[1]

I. INTRODUCTION

Since the European Commission initiated its first leniency program in 1996, such programs have become increasingly popular throughout the European Union, to the point that "the overwhelming majority of the national competition authorities in the 27 Member States [now] operate some form of leniency programme."[2]

After almost two decades of success, however, the level of participation seems to have slightly decreased. While a variety of factors may explain this trend, the most worrying one perhaps relates to the increased disclosure risks associated with private damages litigation.

As a matter of EU law, "any individual has the right to claim damages for loss caused to him by conduct which is liable to restrict or distort competition."[3] In this context, access to evidence is often very valuable for establishing the wrongful act (e.g. the participation in the cartel), the prejudice, and the causal link. This is particularly the case for leniency documents, which are voluntarily produced or submitted by cartel participants to a competition authority with a view to obtaining immunity from fines or a fine reduction. Indeed, a leniency application must generally contain an admission of guilt and a thorough description (and evidence) of the cartel, its scope, duration, functioning, etc. It is therefore not surprising that over the past few years, litigants have repeatedly attempted to access leniency documents, relying either on national law,[4] Regulation 1/2003,[5] or the Transparency Regulation.[6]

Such attempts and the corresponding risks to leniency applicants have led the Court of Justice of the European Union (the "Court") to recognize in *Pfleiderer* that the effectiveness of

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[2] Advocate-General Mazák, Opinion in Case C-360/09 *Pfleiderer* [2011] ECR I-5161 ('*Pfleiderer*'), ¶33.

[3] Case C-453/99 *Courage and Crehan* [2001] ECR I-6297, 24 and 26, and Joined Cases C-295/04 to C-298/04 *Manfredi and Others* [2006] ECR I-6619, ¶¶59 and 61.

[4] *See Pfleiderer*; Case C-536/11 *Donau Chemie and Others* [2013] ECR (not yet reported) ("Donau Chemie"); at national level: Amtsgericht Bonn, judgment of 18 January 2012, Case no 51Gs53/09 (following *Pfleiderer*); High Court of Justice (London), judgment of 4 April 2012, *National Grid Electricity Transmission Plc v ABB,* [2012] EWHC 869; Brno Regional Court, judgment of 23 February 2012, ECLR 2012, 33(6), N81-82.

[5] Article 15(1) of Regulation 1/2003; *see* order in Case T-164/12R *Alstom v Commission* [2012] ECR (not yet reported).

[6] Regulation (EC) No 1049/2001 of the European Parliament and of the Council of 30 May 2001 regarding public access to European Parliament, Council and Commission documents, OJ, 2001, L145/43; Case T-344/08 *EnBW Energie Baden-Württemberg v Commission* [2012] ECR (not yet reported); on appeal: Case C-365/12 P *Commission v Enbw Energie Baden-Württemberg* (pending).

leniency programs could be compromised if leniency documents were to be disclosed.[7] Unfortunately, neither *Pfleiderer* nor the subsequent case law really clarified whether, as a matter of EU law, leniency documents should be disclosed or protected. Ever since, the discoverability of leniency documents and the appropriate balance between the victims' right to compensation under EU law and the attractiveness of leniency programs have raised considerable controversy.

II. PROPOSED DIRECTIVE ON DAMAGES ACTIONS FOR ANTITRUST INFRINGEMENTS

The Commission's proposal for a directive on certain rules governing actions for damages for infringements of competition law (the "Proposed Directive")[8] might clarify where the equilibrium is. The Proposed Directive gives national courts wide latitude in ordering the disclosure of evidence, but also provides absolute protection from disclosure for certain leniency documents.

The Proposed Directive enables national courts to order the disclosure of evidence, regardless of whether that evidence is included in the file of a competition authority. The Proposed Directive also sets out three different levels of discoverability, or "lists":

- the "white" list comprises all those documents which may be disclosed at any time in a damages action;[9]
- the "grey" list concerns information and documents prepared by parties specifically for the proceedings of a competition authority, and materials drawn up by a competition authority during its investigation, which may be disclosed only after the competition authority has concluded its proceedings;[10]
- finally, the "black" list comprises "leniency corporate statements,"[11] which can never be disclosed.[12]

The Commission's proposal to grant the leniency corporate statement such an absolute protection is currently the subject of an intense debate. Within the European Parliament alone, not less than three committees have expressed an opinion. The lead committee—the Committee on Economic and Monetary Affairs—opposes the absolute protection on the ground that it

[7] *Pfleiderer*, ¶¶25-26.

[8] Commission's Proposal for a Directive of the European Parliament and of the Council on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union, COM(2013) 404 final.

[9] Proposed Directive, Article 5.

[10] Proposed Directive, Article 6(2).

[11] Which Article 4(14) of the Proposed Directive defines as any:

> oral or written presentation voluntarily provided by, or on behalf of, an undertaking to a competition authority, describing the undertaking's knowledge of a secret cartel and its role therein, which was drawn up specifically for submission to the authority with a view to obtaining immunity or a reduction of fines under a leniency program concerning the application of Article 101 of the Treaty or the corresponding provision under national law; this does not include documents or information that exist irrespective of the proceedings of a competition authority ("pre-existing information").

[12] Proposed Directive, Article 6(1). The black list also covers settlement submissions. The present discussion will, however, remain focused on leniency documents.

would "create a too far-reaching level of protection."[13] This committee is supported by the Committee on Legal Affairs.[14] However, a third committee—the Committee on the Internal Market and Consumer Protection—takes the opposite view and even suggests that the absolute protection extend to "[a]ll evidence from leniency applicants [...] irrespective of whether they were received in the leniency application or after a request from the competition authority."[15]

The dispute has eventually been resolved in favor of the lead committee's position. As we write, the European Parliament proposes to replace the absolute protection with a limited discoverability of all leniency documents, accompanied with safeguards. The European Parliament is currently defending that position in its discussions with the Council and the Commission. Should the institutions agree on a compromise text, the Proposed Directive could be adopted before the European Parliament breaks up for elections in spring 2014.

This fast-changing legislative context raises the question of whether leniency documents should be "discoverable" at all under EU law, or rather protected from disclosure to third parties. Like Advocate-General Mazák, we "consider that in order to protect both the public and indeed private interests in detecting and punishing cartels, it is necessary to preserve as much as possible the attractiveness of [leniency programs] without unduly restricting a civil litigant's right of access to information and ultimately an effective remedy."[16]

III. PRESERVING THE ATTRACTIVENESS OF LENIENCY PROGRAMS

The vital need to preserve the attractiveness of leniency programs may call for an absolute protection (or non-discoverability) of leniency documents (defined as self-incriminatory documents created specifically for the purpose of obtaining leniency). As explained below, this would serve the interest of both public and private enforcement of antitrust rules.

As regards public enforcement, the Court itself acknowledges that "a person involved in an infringement of competition law, faced with the possibility of such disclosure, would be deterred from taking the opportunity offered by such leniency programmes."[17] As the Court recognizes, the mere possibility of leniency documents being disclosed and used in private litigation discourages, *ex ante*, undertakings from applying for leniency.

Indeed, before applying for leniency, potential applicants always weigh the benefits of immunity against the risks and uncertainties associated with leniency applications (immunity denied or replaced with mere reductions of fines). At that point, a potential liability in damages is

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[13] Committee on Economic and Monetary Affairs, 3 October 2013, Draft Report on the proposal for a directive of the European Parliament and of the Council on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union, PE 516.968v01-00, p. 46.

[14] Committee on Legal Affairs, 27 January 2014, Opinion on the proposal for a directive of the European Parliament and of the Council on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union, PE 524.711v03-00, p. 3.

[15] Committee on the Internal Market and Consumer Protection, 9 January 2014, Opinion on the proposal for a directive of the European Parliament and of the Council on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union, PE 519.553v04-00, p. 3.

[16] Advocate-General Mazák, Opinion in *Pfleiderer*, point 42.

[17] *Donau Chemie*, ¶42, *Pfleiderer*, ¶¶25-27 (emphasis added).

already part of the equation, and no one can really tell how many undertakings prefer to keep their cartel secret because the risks outweigh the expected benefits. Adding an EU-wide disclosure risk to the already complicated equation would not really promote the effectiveness of public enforcement.

It is arguable that disclosure would not promote an effective private enforcement system either. Indeed, unlike in the United States, private enforcement of antitrust rules in Europe depends heavily on public enforcement procedures and resources. The (welcome) absence of a broad U.S.-style discovery mechanism, and the absence of punitive damages, largely explain the need to rely on prior public infringement decisions and initiate "follow-on" actions. In such a context, "[i]f there is no or little detection of anticompetitive behaviour, there are ultimately no victims to compensate."[18]

In sum, the mere possibility of leniency documents being disclosed discourages leniency applications, thereby reducing the potential level of cartel detection and enforcement action, and, ultimately, the likelihood of successful private enforcement across Europe. This is why leniency documents should be protected from disclosure.

IV. PRESERVING "EFFECTIVE" ACCESS TO EVIDENCE FOR LITIGANTS

For the European Parliament, absolute protection would run counter to the main judgments of the Court in *Pfleiderer* and *Donau Chemie*, "as it would violate the principle of effectiveness regarding the right to compensation."[19] The principle of effectiveness is certainly an appropriate benchmark in devising EU legislation on this issue. However, effectiveness, as defined and applied in *Pfleiderer* and *Donau Chemie*, cannot really act as a requirement that would constrain the choices of the EU legislature.

A. Existing Case Law Provides a Benchmark, Not a Legal Constraint

Indeed, in both *Pfleiderer* and *Donau Chemie*, the Court's very starting point was the total absence of any binding EU legislation on either leniency programs or access to national leniency documents.[20] The Court then underlined that it was "accordingly"[21] for the national courts to determine, on the basis of their national law, the conditions under which such access must be permitted or refused by weighing the interests protected by EU law. This is a mere application of the principle of national procedural autonomy, which applies whenever a procedural issue is not governed by express EU legislation.

The sole function of the principle of effectiveness, which the Court recalled,[22] is to limit the national procedural autonomy in the absence of express EU legislation. Accordingly, that principle only applies when and to the extent that no EU legislation governs the procedural rule at issue.

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[18] Committee on the Internal Market and Consumer Protection, *supra* note 15, p. 23.

[19] Committee on Economic and Monetary Affairs, *supra* note 13, p. 26.

[20] See *Pfleiderer*, ¶20, and *Donau*, ¶¶25-26.

[21] *Pfleiderer*, ¶¶23 and 30.

[22] *Pfleiderer*, ¶30.

But the legal situation changes with the Proposed Directive, which aim is, precisely, to expressly govern access to (leniency) documents. The principle of effectiveness cannot therefore be mechanically transposed to the choices made by the EU legislature.

B. Even if Absolute, the Narrowly Defined Protection of Leniency Corporate Statements Reflects a Balanced Approach to Discoverability

Even if the principle of effectiveness could constrain the EU legislature, a further question is whether the absolute protection advocated by the Commission in the Proposed Directive would fall foul of the requirements laid down in *Pfleiderer* and *Donau Chemie*. In those cases, the Court simply laid down a particular requirement that national courts weigh the interests for and against the disclosure of requested documents "on a case-by-case basis, according to national law, and taking into account all the relevant factors in the case"[23] (the "balancing requirement").

Importantly, however, this balancing requirement was set out in relation to a category of documents (leniency documents) that is slightly broader than the one defined in the Proposed Directive ("leniency corporate statements," to the exclusion of all the annexed and related evidence).

Many elements other than leniency corporate statements can prove useful in building a successful damages claim. Claimants can first rely on the infringement decision itself, which generally constitutes—at least—a significant piece of evidence in court. Where the competition authority is the Commission, the infringement decision even binds all national courts as to the existence of a wrongful conduct.[24] Under the Proposed Directive, claimants could also rely on all the evidence annexed to a leniency submission, as well as the raw evidence and statements collected in the course of the investigation.[25] Even the documents specifically prepared for the purpose of public enforcement proceedings[26] would become discoverable, once the competition authority has closed its proceedings.

In other words, under the Proposed Directive, almost the entire case-file would already be discoverable in a follow-on damages action and would be subject to a balancing exercise—a balancing exercise which Article 5 of the Proposed Directive, in fact, imposes on national courts. This Article indeed requires that the claimant presents "reasonably available facts and evidence showing plausible grounds for suspecting" that it has suffered harm caused by the defendant's infringement. The requesting party must also demonstrate that the evidence is relevant to substantiating its claim (or defense) and must define its request as precisely and narrowly as possible on the basis of reasonably available facts. If granted, the order for disclosure must, in any event, be proportionate.

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[23] *Pfleiderer*, ¶31, *Donau Chemie* ¶34. In *Donau Chemie*, the Court applied that latter requirement and declared incompatible with EU law a national provision making access to "documents forming part of the case file of a competition authority" (i.e. a much broader category than leniency documents only) conditional upon the consent of all the undertakings concerned, without leaving any possibility for the national courts of weighing up the interests involved.

[24] *See* Article 16 of Regulation 1/2003; *see also* Case C-199/11 *Otis and Others* [2012] ECR (not yet reported), ¶¶50-51: the legal authority attached to such decisions was at the root of the issues raised (and settled) in this case.

[25] Under Article 19 of Regulation 1/2003 or its equivalent in national law.

[26] Statement of objections and responses, requests for information and responses, etc.

Therefore, the narrowly defined protection of leniency corporate statements still leaves sufficient "room for balancing the public interest relating to effective implementation of competition rules against the private interests of the victims of infringements of the same rules."[27]

C. Effectiveness and (Limited) Added Value of Leniency Corporate Statements

Interestingly, in *Donau Chemie* the Court emphasized that the balancing of the interests for and against disclosure had to be made "in the light of other possibilities [claimants] may have."[28] Given the narrowly defined protection of leniency corporate statements and the numerous "other possibilities" listed above, the question arises as to whether the added value of such statements is so important.

On the one hand, a leniency corporate statement may prove helpful because it structures the presentation and understanding of the evidence contained in the case file. A leniency corporate statement may thus help to make the evidence "talk" in court. On the other hand, the extent to which such a document actually helps is also extremely variable, depending on all the other—discoverable—elements: the length and detailed nature of the infringement decision, the type of evidence, etc.

Therefore, without denying that leniency corporate statements may help victims prove their case in courts, one fails to see what would be systematically so crucial about these documents that their absence would render the claim "practically impossible or excessively difficult" within the meaning of the effectiveness principle recalled in *Pfleiderer* and *Donau Chemie*.

Finally, it may be worth recalling that the Proposed Directive would, for the first time, establish an EU-wide litigation platform comprising common substantive and procedural rules. Removing the current discrepancies between Member States regarding, *inter alia*, the disclosure of evidence, already constitutes a huge step forward for the private enforcement of antitrust rules. In such a context, and whatever the exact added value of leniency corporate statements, the private enforcement of antitrust rules can only be more effective, once the Proposed Directive is adopted.

It is very difficult to conceive that the legal status of leniency corporate statements, alone, could neutralize such progress. Indeed, the recognition that various documents prepared by parties specifically for the proceedings of a competition authority (the so-called "grey" list) can become discoverable once those proceedings are closed has some commentators saying the Proposed Directive (if adopted) will chill leniency applications as it is taking disclosure too far in favor of private litigants.

V. CONCLUSION

In sum, we side with the Commission and believe that only an absolute protection for certain narrowly defined leniency documents will strike the right balance between the need to preserve the attractiveness of leniency programs and the need to maintain the effectiveness of the

[27] Advocate-General Jääskinen, Opinion in *Donau Chemie*, ¶69.
[28] Donau Chemie, ¶24.

right to damages for victims.[29] Provided that such protection remains limited in scope, it will not deprive the victims' right to compensation of any effectiveness.

The "balance" could be there: The protection of leniency corporate statements may be absolute, but it remains limited in scope.

[29] A position apparently shared by Advocate-General Jääskinen himself: *see* his Opinion in *Donau Chemie*, ¶64.

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Recent Trends in Leniency Agreements in Brazil

Barbara Rosenberg, Marcos Exposto, Sandra Terepins & Luiz Galvão

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Recent Trends in Leniency Agreements in Brazil

Barbara Rosenberg, Marcos Exposto, Sandra Terepins & Luiz Galvão[1]

I. INTRODUCTION

For the past two decades, leniency programs have been growingly adopted by antitrust authorities around the globe as one of the main tools in cartel prosecution. As seen in other jurisdictions, the Brazilian authorities have been striving to build a well-respected leniency program. The last couple of years suggest that the Brazilian competition authority—the Administrative Council for Economic Defense ("CADE")—in order to grant the benefits of the leniency program has been gradually more demanding regarding the need to collect strong evidence of the existence of a collusion, as well as proof of (potential) effects in the country.

Based on recent experience, the standard of what is considered acceptable to secure an agreement seems to be higher than it was in the past, when leniency agreements were accepted in any global cartel case under the presumption that it *could* have generated effects in Brazil. This new trend— only accepting leniency applications for cartels that are effectively proven to have effects in the Brazilian market—is clearly welcome from a policy standpoint.

II. HOW THE LENIENCY PROGRAM FUNCTIONS

The leniency program was launched in Brazil in the year 2000 and, albeit subject to minor changes, remains in force under the recent Antitrust Law, Law no. 12,529/2011 and respective regulations. CADE may execute leniency agreements in cartel cases and is represented for that purpose by its Superintendence General ("SG"), CADE's investigation division.[2]

A company that applies for leniency in Brazil may receive full administrative immunity or a fine reduction (varying from one- to two-thirds of the imposed penalty), plus full criminal immunity for individuals (in Brazil, only individuals are criminally prosecuted for cartel offenses). Full immunity is available if, at the time the leniency application is presented to CADE, the authority had no previous knowledge of the reported conduct and had not started any investigations. If there is an already ongoing investigation (which may be started by the authority spontaneously or pursuant to a third-party complaint), but at the time of the leniency application CADE did not have sufficient evidence to guarantee the conviction of the defendants, partial immunity can be available and can result in a reduction of the fines, as indicated above.

In both cases, individuals will not be criminally indicted and, once the obligations undertaken as a result of the leniency agreement have been fulfilled, any risk of penalties

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[2] Recently, Law no. 12,846/2013 brought the possibility of leniency agreement executions regarding corruption practices. The possibility is still at an early stage since it lacks important aspects of the antitrust leniency program, such as a well-defined authority responsible for receiving the agreement and confidentiality rules for the documents and information submitted.

(administrative and criminal) is excluded. It is important to highlight, however, that under no circumstance does the leniency agreement provide immunity for damage claims from third parties that may have been victims of the cartel.

In order to have a leniency agreement proposal accepted by CADE, some legal requirements must be met: the beneficiary must: (i) be the first to come forward and report the conduct; (ii) immediately cease its involvement in the practice; (iii) confess to its participation in the conduct; and (iv) cooperate with the whole investigation. Likewise, the SG must *not* have sufficient evidence to start the investigation without the beneficiary's proposal and, as a result of the cooperation, the SG must be able to identify other companies and individuals involved and receive sufficient evidence to convict them.

III. QUALIFYING EFFECTS IN THE NATIONAL MARKET

The first leniency agreement was executed in 2003, in a case involving a domestic bid-rigging case in Southern Brazil. Since then, the program has evolved considerably. In the beginning, perhaps due to a mindset of consolidating Brazil's place in the "leniency world map," several investigations were initiated based on leniency agreements that did not contain clear evidence of having an impact in Brazil. This may have been a result of the authorities' eagerness to build a reputation of active enforcement—but it had the downside of starting cases that were not very strong (at least with respect to the effects in Brazil). In some of these early cases, the Brazilian authorities adopted a very broad interpretation of what qualified as *effects* in the national market and even stated that they were opening the cases to *assess* the existence of effects.

As an example of CADE's experience, it is worth mentioning the *Vitamins' Case*[3]—one of the first and most paradigmatic precedents in Brazil regarding an international cartel investigation. Even though the case did not start with a leniency agreement, it is a good example of how CADE dealt with the effects discussion in the early days of the prosecution of international cartels in Brazil.

In the *Vitamins' Case*, the investigations were started based on public information made available by foreign antitrust authorities about their own investigations suggesting that the investigated cartel was worldwide in scope. Even though general references to Latin America were found in the documents made available by foreign authorities, the case records did not contain either specific references to the Brazilian market or to agreements or contacts among cartel members targeted at Brazil.

Regardless, the authorities assumed that the practice at hand would have effectively affected the Brazilian market by taking into account that: (i) there was virtually no local production of vitamins in Brazil; (ii) the investigated companies were responsible for a significant part of vitamins market in Brazil by means of imports by local subsidiaries; (iii) the companies had been convicted in other jurisdictions for engaging in a cartel with international scope; and (iv) according to the depositions taken from the local employees, the prices in Brazil were established by the companies' headquarters. No Brazilian employees were implicated, as CADE understood that they were not aware or involved in the practice, which was entirely conducted abroad.

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[3] Administrative Proceeding 08012.004599/1999-18, closed on April 11, 2007.

According to recent statements from the CADE, however, this approach has changed over the past couple of years.[4] In fact, there has been no public information about cartel investigations being initiated in the last years on the basis of mere press releases issued abroad, as had happened with the following investigations: *Graphite Electrodes case*,[5] *LCD case*,[6] *DRAM case*,[7] and *Vitamins Case*. Likewise, following the same trend of requiring more nexus with Brazil prior to assuming an impact in Brazil by global cartels, the authority has been requesting more information from the applicants, including stronger and direct evidence of the cartel relating to Brazil. This shift in demand seems to be a natural transition and proves that the Brazilian antitrust authority is at a more developed stage.

The documents and evidence that must be presented by the applicant of a leniency agreement gain even more importance regarding international cartels. In order to sign a leniency agreement, CADE usually now requests direct evidence that the cartel produced effects in the Brazilian market. It does not mean, however, that the authority is trying to create difficulties for the execution of leniency agreements. On the contrary: The fact that CADE is demanding more information and evidence from leniency applicants suggests that the authority is being more careful when deciding whether start an investigation, requesting concrete evidence rather than circumstantial elements.

By being more cautious when accepting leniency applications, the authority is making sure they have stronger cases. Even though it may seem more difficult for companies to execute leniency agreements with CADE in the beginning, this means that leniency agreements will have a greater chance of being successful in the future.

In light of this change in approach, it seems clear that the Brazilian leniency program designed by the Brazilian Law is on the right track. The leniency program model should become even more successful to the extent the authority is cautious when executing the agreements.

In international cartel cases, CADE has also been claiming to drop leniencies when there is not a clear nexus between the conduct and effects in the Brazilian market. CADE seems to be more cautious when using information from other jurisdictions in international cartel cases, such as leniency agreements executed in other countries and decisions from other authorities. Even though it was previously possible to see leniency agreements being executed based merely on other countries' decisions, plea agreements, and other documents related to foreign jurisdictions, documents like these are no longer expected to be considered sufficient to start an investigation in Brazil. When considering a leniency application in Brazil, a company will need to provide evidence other than foreign leniency agreements and foreign decisions in order to demonstrate that the practice affected the Brazilian market.

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[4] Carlos J. E. Ragazzo, CADE's General Superintendent stated in April 2013 that "We are not going to have 200 cartel investigations anymore. The ones that we do [pursue] are going to have a very high probability of conviction and they will be very, very sturdy cases" (*See* A. Rego, *CADE redefining focus of cartel enforcement*, MLex, published on 8 Oct 13 | 20:11 GMT). The same article mentions that a spokesperson for CADE suggested that "[in respect to] international cases, CADE has sought to be more rigorous—that is, we have looked for cases in which the proof of the effect or the potential effect [of the cartel] is clear."

[5] Administrative Proceeding # 08012.009264/2002-71, initiated in May, 2009.

[6] Administrative Proceeding # 08012.011980/2008-12, initiated in December, 2009.

[7] Administrative Proceeding # 08012.005255/2010-11, initiated in June/2010.

An important example of how CADE has been dealing with evidence gathered though leniency agreements is the *Air Cargo* case,[8] the first decided case involving an international cartel in Brazil which investigation was started pursuant to a leniency agreement. The case started with the execution of a leniency agreement, and, in the context of cooperation, the beneficiary provided CADE not with only copies of leniency agreements and decisions from other jurisdictions, but also with alleged evidence that the cartel would have actually affected the Brazilian market. Even though the agreement was signed not very long after leniency agreements became acceptable in Brazil, it can be seen as a good example of CADE's recent approach when taking into account evidence for a cartel investigation.

The more cautious CADE gets with the evidence it collects before initiating an investigation (through a leniency agreement or not), the more the defendants seem to be willing to execute agreements to cooperate with the authorities and pay fines before the administrative proceeding is finally finished. In most cases, executing agreements with the defendants can be advantageous to the authority, since: (i) the agreement reduces the chances of having its decision contested in court; and (ii) the authority gathers more evidence of the conduct—as a result of mandatory collaboration—which may strengthen its final decision. That was seen in the above-mentioned *Air Cargo* case, which started with the execution of a leniency agreement and was followed by a defendant executing an agreement with CADE in which he confessed the practice and agreed to pay a considerate amount of money to CADE.

IV. CONCLUSION

Therefore, it is possible to say that CADE has been adopting a more cautious approach when reviewing applications for leniency agreements. In the early days of the leniency program in Brazil, CADE seemed to be more focused on developing a leniency program and on gaining recognition for the program rather than in executing agreements based on strong evidence of effects of the conduct in Brazil. By behaving that way, companies might have come to the perception that CADE was adopting an overly broad approach of effects of a supposedly illegal practice in Brazil and may have been influenced to go forward to disclose an illegal practice, even with not-so-clear effects in Brazil. By now giving signs in the opposite direction—i.e. having indicated a more demanding and cautious approach as regards evidence and standard of proof, CADE seems to be building a more solid and mature leniency program. The shift is especially important when international cartels are at stake.

These developments should not represent any additional burden on companies willing to blow the whistle, nor should they be construed as an indication that the program itself will be less successful. Conversely, the authorities seem to seek legal certainty and wish to drive their energy and sources to cartel cases that prove to have a negative effect in the Brazilian market. The more cautious and precise the authority is during the negotiation of a leniency agreement, the stronger the cases that are brought. In sum, the welcome change in CADE's behavior means that the authority is finally achieving a more mature stage in its policy development.

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[8] Administrative Proceeding 08012.011027/2006-02, closed on August 28th, 2013.

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The Finnish Asphalt Cartel Court Decision On Damages: An Important EU Precedent And Victory For Plaintiffs

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The Finnish Asphalt Cartel Court Decision On Damages: An Important EU Precedent And Victory For Plaintiffs

John M. Connor & Toni Kalliokoski[1]

I. INTRODUCTION

During 2002-2004, the Finnish Competition Authority ("FCA") investigated the National Road Administration ("NRA"),[2] seven construction companies, and their trade association for bid-rigging road asphalt projects over an eight-year period. According to the FCA, affected sales were about $2.17 billion.[3] The FCA considered the companies and their association guilty of illegal cooperation in bidding, allocation of markets, exchange of sensitive business information, and preventing entry of new suppliers, but did not press charges against the NRA because of lack of evidence.[4]

In 2004, the FCA proposed to the Market Court a fine of EUR 92 million ($122 million), of which the cartel's leader Lemminkäinen Oyj was to pay 70 percent. Three years later that court issued a decision that severely reduced the proposed fines, but it was overruled by the Supreme Administrative Court in late 2009, which imposed fines of EUR 82.6 million ($124 million), of which Lemminkäinen Oyj was to pay 82 percent. These are by far the highest antitrust fines in Finland's history.

After the Supreme Administrative Court's judgment, an antitrust damages trial ensued in the Helsinki District Court in which the State of Finland and 40 cities and towns made claims of EUR 120 million against the privately owned construction companies. The ensuing trial was by many measures the largest civil proceeding ever seen in Finland's courts.[5] The District Court's

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[1] The first author is Professor Emeritus at Purdue University, West Lafayette, Indiana and Senior Fellow of the American Antitrust Institute; the second author is an attorney with the law firm Dittmar & Indrenius, Helsinki, Finland; author of the first book in Finnish about antitrust damages actions; and an attorney who litigated this case for municipal plaintiffs.

[2] The NRA is the state agency responsible for public roads in Finland. As part of its responsibilities, it commissions road production services from service providers.

[3] The $2.17 billion figure is based on a June 2003 FCA press release that said that the sales of the defendants (including at the time the Finnish State) in 2002 were EUR 355 million. (This number is also consistent with The FCA's Fining Proposal of 31 March 2004, p. 14, where total national sales in 2002 are stated to be EUR 392 million and the cartel controlled 90% of national supply). We assumed conservatively a 5 percent p.a. nominal growth rate and added the years 1995-96 and 1998-2002 together. The total was EUR 2.089 billion; converted into dollars each year, the total become $2.1709 billion (with no adjustment for inflation). Actually, the total market would be $2.412 billion because the cartel, as it was then defined, controlled only 90 percent of the Finnish market, but it is likely that the remaining 10 percent was affected by umbrella pricing.

[4] Unlike the European Commission, the FCA cannot make a finding of infringement. The FCA is more like a prosecutor and can only propose that the Market Court make a finding of an infringement and impose fines.

[5] The case was heard by a panel of three judges, which is normal in large cases. There were 41 plaintiffs and eight defendants. The plaintiffs were represented by eight law firms, except for four of the municipalities that represented themselves. The defendants were represented by six law firms. Total legal fees and costs demanded by the parties were approximately EUR 17 million.

Written and oral preparation took three years, during which over 2,000 documents were submitted as evidence.

decision of November 28, 2013 is the first cartel antitrust damages judgment in the history of Finland.[6]

II. OVERVIEW

From a legal point of view, the judgment was a nearly complete victory for the municipalities, but the Finnish State's[7] claim was dismissed for reasons discussed below. From a damages point of view, due to the addition of two types of interest the amounts awarded typically exceeded the overcharges by more than 50 percent.

The decision established a reasonable and coherent basis for awarding antitrust damages in Finland and may be influential across the European Union. The decision may also be seen as somewhat plaintiff-friendly, but much of the Court's reasoning was, ultimately, based on common sense. Further, from a monetary point of view, the decision could also be viewed as a strategic victory for the defendants because they managed to substantially reduce the total damages by having the Finnish State's claim completely thrown out.

The District Court's decision is still subject to appeal. Many of the legal questions are such that ultimately the Supreme Court may wish to rule on them.

III. OVERCHARGES

For almost all the municipalities the Court applied an overcharge of either 15 or 20 percent of the size of the asphalt project (i.e. affected sales), depending on the price evidence presented. Thus, compared to the hypothetical competitive price, the typical overcharges were either 18 or 25 percent of the bids.

The Court used 15 percent as the presumptive overcharge unless it was proven otherwise. The choice of the percentage was mostly based on the plaintiffs' economic expert analysis and the testimonies of witnesses who had worked for the cartel companies at the time of the cartel. Those plaintiffs who could show sufficient evidence for higher overcharges received 20 percent. On the other hand, for one plaintiff the actual asphalting contracts showed no price increase over 1990–2001, and its claim failed.

A Ministry of Finance report issued in 2006 made a rough estimate of total asphalt-cartel overcharges.[8] The report took affected sales by the privately owned asphalt companies to be EUR 290 million in 2002 and adopted a 20 percent overcharge, which it regarded as slightly

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The parties submitted over 30 expert reports on the amount of damages or the interpretation of the law. The main hearings took seven months, mostly three days a week. The court heard 66 witnesses. Most of the expert witnesses were Finnish but two were not. When the court heard them, there was a translator present. Some of the counsel did their own translating, as they had prepared the questions both in Finnish and in English.

In an unusual move the court wanted to hear first from the parties to make their arguments concerning points of law. This is not normally the case because courts already know the law. In this case, the parties spent two months at the beginning of the main hearings arguing about the correct interpretation of the law with regard to the numerous precedent-setting questions.

[6] There are 41 separate judgments, e.g., Helsinki District Court judgments 13/64901 (the State of Finland), 13/64913 (the City of Helsinki, Finland's capital), and 13/64929 (the City of Espoo, Finland's second largest city).

[7] In American parlance, this would be termed the National Government of Finland.

[8] Ministry of Finance. *Talouspolitiikan strategia -raportti 2006*, p. 65. (May 31, 2006).

conservative.[9] For the eight years, total national monetary losses (and the seller's monopoly profits) were projected to be roughly EUR 464 million ($478 million).[10] Given the Court's findings on actual overcharges for municipalities, this estimate appears to be quite close to one that might have been made with the Court's blessing.[11]

IV. AMOUNT OF DAMAGES

The Court identified two cartel phases. The first phase was 1994-1995 and the second 1998–2001 or -2002. The years 1996-1997 were marked by a price war, so plaintiffs generally received no compensation from those years unless they could prove the price war had not affected them.

The total "capital" (i.e., pure compensation) of the damages awarded to 39 of the 40 municipalities was EUR 37.4 million ($50.8 million). However, interest increased the total awards considerably. For some claims, the capital was increased by a third by *compensatory* interest that accrued from the time the overcharge was paid in 1994-2002 up to the time that the claims were lodged.[12] In addition, *punitive* interest of about 10 percent per year further accrued on the capital and the compensatory interest from the time the claims were lodged. Finally, defendants will have to pay plaintiffs' reasonable attorney's fees. For many of the smaller towns, legal fees exceeded capital awards, but for the city of Helsinki representation cost less than 4 percent of capital awards.[13] All these amounts are given for each claim in the Appendix to the Court's Press Release (see below).

The total amount awarded to the municipalities was approximately EUR 60 million ($81million).[14] The components were: EUR 34 million in "capital," EUR 20 million in interest,

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[9] The Ministry of Finance cited three publications as authorities for this average overcharge figure: (1) John M. Connor & Robert H. Lande *How High Do Cartels Raise Prices? Implications for Optimal Cartel Fines*, (80) TULANE L. REV. 513-570 (December 2005); (2) John M. Connor & Yuliya Bolotova, *Cartel Overcharges: Survey and Meta-Analysis*, (24) INT'L J. IND. ORG. 1109-1137 (Nov. 2006); and (3) John M. Connor, *Price-Fixing Overcharges: Legal and Economic Evidence*, RESEARCH IN LAW AND ECONOMICS. VOL. 22, Ch. 4, 59-153 (John B. Kirkwood, ed., January 2007).

[10] These are income-transfer losses only and do not include dead-weight social losses. Nor do they include sales by State-owned asphalt plants, which the Court decided to exclude (see Section 6 below).

[11] It is possible that because of its bargaining power, the central government purchases (38 percent of the total) might have enjoyed a lower overcharge rate, but smaller private buyers (34 percent) would likely have experienced the opposite. Thus, on balance, the 20 percent rate adopted is a decent compromise for the overcharges on all three customer types. Data on customer shares are taken from Finnish Competition Authority, *FCA Proposes Heavy Fines for Members of Asphalt Cartel: News Release* (31 March 2004) [www.kilpailuvirasto.fi/cgi-bin/print.cgi?/sivu=news%2Fn-2004].

[12] The date at which the claims were lodged was an issue in the litigation. The Court did not accept plaintiffs' arguments for an early date. This part of the Court's decision slightly reduced the plaintiffs' awards because the rate of interest on compensatory interest was very low compared to the punitive interest of about 10 percent per annum.

[13] Note that, unlike the case of contingent fees in class actions, in Finland fees are not subtracted from the total award; rather, they are assessed separately by the Court upon defendants.

[14] Note that the plaintiffs asked for EUR 66 million in compensation, almost double the amount awarded as capital. In retrospect, the amount of compensation requested was a bit low because some of the plaintiffs believed that the first phase of the affected period (1994-1995) was time-barred and did not make claims for those years. In other cases, plaintiffs' claims were based on evidence of overcharges above 20 percent and as high as 30 percent, the latter of which the Court disallowed.

and EUR 6 million in attorneys' fees. The 40 municipalities that made claims represent about 50 percent of the Finnish population living in towns and cities. Thus, these claimants suffered injuries of about EUR 66.9 million (in 1998 euros).[15]

As the award is about 60 percent of plaintiffs' damages,[16] the EUR 60 million awarded (in 2013 euros)—if it were to be paid immediately by the defendants—would not entirely disgorge the profits made by the cartel.

V. ECONOMIC ANALYSIS

Analysis by economic experts was central to the case. Experts for the plaintiffs found an unexplained and statistically significant price increase of roughly 20 percent that they attributed to the cartel. However, experts for the defendants found no statistically significant price increase, and some of them found that the bids submitted by Lemminkäinen Oyj were, on average, lower during the cartel period than afterwards.

The Court found the results of the defendants' experts less convincing because they went against all other evidence, which showed the cartel to have been effective in charging higher prices. Furthermore, the defendants' experts appeared to blunder by including both winning bids and unsuccessful bids in their data, but could not identify which were which.[17] The Court found that this compromised the quality of the data and raised questions concerning the selection of the data that was provided to the experts.

The evaluation of econometric evidence was clearly very difficult as the Court wrote more than 60 pages discussing it in the judgment. This is an enormous amount of written discussion; Finnish courts normally write very short judgments that include little or no commentary. The Court also cited empirical overcharge studies, such as the analysis in the Oxera report for the EU Commission, which was based on data supplied by John Connor.[18]

VI. THE STATE'S FAILURE

The capital awards fall far short of the EUR 120 million ($163 million) claimed by the plaintiffs, mostly due to the total failure of the Finnish national government's case. The complete failure of the Finnish State's claim was a great surprise. Recall that the FCA had not charged the NRA (a state agency) with complicity in the cartel. Therefore, observers were expecting that even if the State were found to have known about the cartel, or participated in some part, it might have had its damages reduced, but not its whole claim thrown out.

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[15] Here is the arithmetic: Total national compensable losses are EUR 464 million (measured on average in 1998 euros). Towns and cities purchased 28 percent of the total or EUR 133.8 million, of which the 40 plaintiffs represent approximately 50 percent of those purchases or EUR 66.9 million. Assuming a modest 3 percent rate of general inflation from 1998 to 2013, that EUR 66.9 becomes EUR 104.3 million in 2013 euros.

[16] There are pending claims of about EUR 8 million. However, judging by the success of the first wave of claims, the capital is likely to be reduced by at least a third or a half. A still greater number of municipalities are waiting for the final outcome from the Supreme Court, where the case will likely end up. After that, they will make their claims if the case is favorable to them. So, the total could still increase.

[17] The experts asked their clients for all possible transactions, but Lemminkäinen could not distinguish winning from losing bids.

[18] Oxera Consulting. *Quantifying antitrust damages: Towards non-binding guidance for courts Study prepared for the European Commission.* Luxembourg (December 2009).

In 1998, the NRA had been organizationally split into production and procurement departments.[19] The procurement department decides what asphalting services the State needed and requests tenders. The production department provides some of those asphalting services using its own capacity and subcontracts some of it from private companies. It was shown that some people in the production department knew about the cartel and had even participated in it to some extent. The procurement department was not shown to have known about the cartel.

However, the Court considered the State an indivisible entity, so the State in its entirety was considered to have known about the cartel. As such, the Court considered that the State was not entitled to any damages. Moreover, like all losers, it was required to pay legal costs to defendants in the amount of EUR 2.6 million ($3.5 million).

VII. DOCTRINE OF ECONOMIC SUCCESSION

Another great surprise was that the Court adopted the doctrine of economic succession into antitrust damages. In public enforcement it is well accepted in the European Union that the economic successor of a company is liable to pay fines for the conduct of its predecessor if the predecessor no longer exists. It is not possible to evade liability, e.g., by selling the infringer's assets to a new company and liquidating the infringing company. However, no such doctrine seems to apply in the European Union for antitrust damages. By comparison, in the United States and other Common law jurisdictions, liability is determined by the merger contract or state of incorporation.

In the asphalt cartel damages litigation, some of the defendant companies had not participated in the cartel. They had purchased certain companies that had participated in the cartel, transferred the assets of those cartel companies to themselves and they subsequently liquidated those cartel companies. This seemed to leave no suitable defendant under Finnish law, thereby denying an effective remedy from a number of plaintiffs.

However, the Court considered that EU antitrust legislation and ECJ case law compelled the Court to ensure that national law provides effective antitrust damages remedies for breaches of EU antitrust law. Since national law prevented an effective outcome, the Court ignored the national law and applied EU law directly. Thus, the Court applied the EU antitrust law doctrine of economic succession into antitrust damages. This was apparently the first time this doctrine was applied in an antitrust damages case, representing a significant new interpretation by the Court.

VIII. CONCLUSIONS

In the *Finnish Asphalt* case the Court provided considerable direct compensation for the 40 municipalities that sued and also relief in the forms of two types of interest payments and substantial legal fees for plaintiffs' attorneys. After laboriously weighing complex economic, statistical, and testimonial evidence, the Court boldly chose to agree with the economic analysis of plaintiffs on the size of the overcharges, rather than simply choose some number in between

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[19] The NRA owns and operates its own asphalt plants for surfacing national roads. This is the responsibility of the production department. However, the NRA's own capacity was insufficient for the total asphalting needs, so the procurement department purchased additional asphalt supplies from the defendants.

the two positions.[20]

We believe that the Court closely and consciously adhered to EU-wide principles of law; but, at the same time, the case broke new ground by offering to plaintiffs seeking redress in private antitrust damages suits a model decision that had features that could achieve full compensation. These included: lenient rules on time-barring; patient weighing of economic, documentary, and testimonial evidence; severe interest penalties to compensate victims for the time value of money; and generous legal fees for plaintiffs' attorneys (preferably with a risk reward recognized).

However, the deterrence power of this private action was limited by three factors. First, because the Court considered the national state indivisible, and because some officials in the National Road Administration were aware of the asphalt cartel's existence, the Finnish State's right to compensation was forfeited[21] Thus, taxpayers went uncompensated for overpayments on asphalting of public roads. Second, there are more than 300 municipalities in Finland, yet only 40 of them chose to sue. Smaller towns could not afford to sue because legal fees were likely to be large (the loser pays) and class actions are not feasible under Finnish law. Third, because of the great uncertainty of winning in absence of precedents, no private businesses sued the asphalt cartel, and they are unlikely to do so. For these reasons, approximately 75 percent of the monopoly profits of the *Finnish Asphalt* cartel could not be legally recovered through civil damages actions.

This decision is noteworthy for several other reasons:

- The eight-year-long Finnish asphalt cartel was extremely injurious, with at least $478 million in total market overcharges and tens of millions more in net social losses. In 2009, the young Finnish Competition Authority achieved a solid legal victory in the courts by obtaining a record-setting $122 million fine on this cartel.
- Plaintiffs' attorneys and economic experts were able to persuade the Helsinki District Court to adopt many novel and complex legal-economic concepts, the result being a bold and sophisticated template for EU courts elsewhere.[22]
- The Court's decision was very favorable for larger municipal plaintiffs, but because of an undeveloped class action or representative-action system of law, smaller claims could not be filed.

[20] We believe that this is what happened in the *District Heating Pipes* private litigation in Denmark. (We suspect that many courts, when faced with conflicting economic testimony that they do not feel competent to reconcile, often are tempted to "split the difference.") Interestingly, in contrast to Finland, the Danish Court chose to ignore evidence that municipalities had colluded with the steel companies that supplied them with over-priced pipes. Given the conflicting rulings between the Danish and Finnish courts on the role of government participation in bid-rigging, the European Court of Justice may wish to take up this issue.

[21] One wonders how far the Court is likely to go in pressing this principle, because the Competition Authority itself is also part of the state.

[22] The decision about disallowing the Finnish State's claim may well be *sui generis* to this case. However, the authors are aware of credible press reports of allegations of the active involvement of government officials in construction bid-rigging cartels in Sweden, Poland, Japan, and other nations.

- The additional $81 million in payments may provide significant additional dissuasion for future cartels, but by allowing the cartel to retain almost 60 percent of its illegal monopoly profits, cartel deterrence is surely sub-optimal.

IX. ADDENDUM: HELSINKI DISTRICT COURT PRESS RELEASE, 28 November 2013

HELSINKI DISTRICT COURT

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ASPHALT CARTEL TRIAL CONCLUDED AT HELSINKI DISTRICT COURT

On the proposal of the Finnish Competition Authority, the Supreme Administrative Court ordered on 29 September 2009 Lemminkäinen Oyj, VLT-Trading Oy, Skanska Asfaltti Oy, NCC Roads Oy, SA-Capital Oy, Rudus Asfaltti Oy and Super Asfaltti Oy to pay a total of EUR 82.55 million of what are called infringement fines for their participation in a cartel that operated on the Finnish asphalt market in 1994-2002.

In 41 claims for damages brought at the Helsinki District Court, the State of Finland and 40 local authorities have claimed compensation from above mentioned companies and one other company for the overcharges they have paid for paving work. The companies have contested the claims. Judgments in the matter were announced today.

Claim for damages by the. State of Finland

The State (Finnish Transport Agency) has claimed a compensation of EUR 56.7 million in total from the companies. The District Court has *dismissed* the action by the State in its entirety, and has obligated the State to compensate the companies for their legal costs by the total sum of EUR 2.6 million.

The District Court has received partly new evidence after the trial at the Supreme Administrative Court, and the District Court has found that the National Board of Public Roads and the Finnish Road Enterprise participated in a cartel concerning work commissioned by the State from the year 1998 at least. In addition, representatives of the National Board of Public Roads have been aware of the existence of the cartel as early as in 1994. The District Court considers that no damage has been caused to the State on the basis of the activity which the State has approved at the time when it took place, which the State has participated in, and from which the State itself considers to have benefited from.

Claims for damages by Local Authorities (40 claims)

The claims by the local authorities have been *allowed* for the most part. Appended to this media release there is a list of the local authorities, their claims on capital, the percentages of overcharges paid and the capital sum of the damages awarded, a total of EUR 37.4 million. The interest based on rate of return and penal interest add considerably to the amount of damages awarded. The local authorities mostly have been overcharged by 15% for asphalt work; some by 20%. In 1996-1997, a period of a price war prevailed in Finland, and contracts concluded during these years did not usually involve overcharging.

Appended to this media release are the judgments concerning the cities of Helsinki and Espoo. The judgments concerning other local authorities (in Finnish) may be obtained from the District Court (sari.harma@oikeus.fi).

Court Proceedings

The claims became pending in 2008-2011. After preparation in writing, the District Court arranged two joint preparatory hearings, separate preparatory hearings for each claim during spring 2012 and a joint main hearing of seven months' duration in 2012-2013. More than 2,000 documents were submitted as evidence and 66 witnesses were heard during the main hearing. The combined number of pages in the judgments comes up to about 10,000.

The economic evidence related to the causes of cartel damage was extensive. Both plaintiffs and defendants had several studies made on the damage, in addition to which, hearing the testimonies of the expert witnesses took about one month.

Competition law is a strongly binding area of EU legislation; furthermore, the right of everyone to receive compensation for damage caused by infringements of competition law has been confirmed by the EU courts. The importance of EU law is emphasised parallel to national law despite the fact that the claim for damages is dealt with by national courts. Throughout the 2000s, the Commission of the European Union has made efforts to promote the enforcement of the right to damages. However, due to difficulties related to submitting evidence, among other things, trials involving claims based on competition law have so far been infrequent in Europe. Consequently, the extensive asphalt cartel trial in Finland has attracted the interest of the Commission and the other Member States of the EU.

The Helsinki District Court was the first in Finland to use videoconferencing during the main hearing. During the asphalt cartel trial, instead of travelling to Helsinki three to four times a week during the seven-month main hearing, attorneys from law offices from outside Helsinki took part in the hearing via video links from their own localities. Up to ten attorneys at a time took part in the main hearing in this way. This procedure led to a considerable decrease in the trial costs of the parties.

Fourteen other claims are still pending at the District Court, in which local authorities claim damages for overcharging. Over 700 claims dealing with a timber cartel are also waiting to be processed by the Court. To date, the District Court has not been assigned the personnel resources needed for processing these by the Finnish Ministry of Justice.

Appendix 1a

Appendix to Media Release 28 November 2013/ Claims for damage in asphalt cartel matter 1

Plaintiff **-** Defendant(s)	**Capital Claim**	**Capital Sum Awarded**	**Percentage Overcharged**	**Legal Costs**
Espoo - Lemminkäinen Oyj - Skanska Asfaltti Oy -VLT Trading Oy estate in bankruptcy - NCC Roads Oy - SA-Capital Oy - Rudus Asfaltti Oy - Super Asfaltti Oy	**5.319.944,14 euro** - joint and several liability in part	**1.843.227,37 euro** - joint and several liability in part	**15,00 %**	**490.000 euro** - joint and several liability in part
Forssa - Lemminkäinen Oyj	**602.065 euro**	**267.200,19 euro**	**15,00%**	**190.000 euro**
Haapajärvi - Lemminkäinen Oyj	**57.937,14 euro**	**28.968,58 euro**	**15,00%**	**210.000 euro**
Helsinki -Lemminkäinen Oyj -VLT Trading Oy estate in bankruptcy	**14.065.717,76 euro** - joint and several liability	**9.274.691,05 euro** - joint and several liability	**20,00%**	**339.000 euro** - joint and several liability
Hollola - Lemminkäinen Oyj	**453.578 euro**	**175.371,22 euro**	**15,00%**	**160.000 euro**
Hyvinkään - Lemminkäinen Oyj	**1.426.586,50 euro**	**586.011,61 euro**	**15,00%**	**117.000 euro**

Appendix 1b

Appendix to Media Release 28 November 2013/ Claims for damage in asphalt cartel matter 2

Iisalmi -Lemminkäinen Oyj -VLT Trading Oy estate in bankruptcy	**830.304,64 euro** - joint and several liability	**39.507,94 euro** - Lemminkäinen Oyj **196.925,92 euro** - VLT Trading Oy	**15,00%**	**115.000 euro** - joint and several liability in part
Imatra - Lemminkäinen Oyj	**698.608 euro**	**523.955,77 euro**	**15,00%**	**42.000 euro**
Joensuu - Lemminkäinen Oyj	**530.349 euro**	**353.566,88 euro**	**20,00%**	**165.000 euro**
Jyväskylä - Lemminkäinen Oyj	**2.006.215,82 euro**	**1.506.346,05 euro**	**15,00%**	**64.000 euro**
Kaarina - Lemminkäinen Oyj	**1.132.947 euro**	**568.644,17 euro**	**20,00%**	**87.000 euro**
Kajaani -Lemminkäinen Oyj -NCC Roads Oy -Interasfaltti Oy	**688.627,48 euro** - joint and several liability	**270.194,58 euro** -Interasfaltti Oy and NCC Roads Oy joint and several liability Claim against Lemminkäinen Oyj is dismissed.	**15,00%**	**194.000 euro** -Interasfaltti Oy and NCC Roads Oy joint and several liability **35.504,70** - Kajaani pays Lemminkäinen Oyj
Kemi - Lemminkäinen Oyj	**1.152.528,76 euro**	Claim is dissmissed.	----	**45.949,60 euro** - Kemi pays Lemminkäinen Oyj

Appendix 1c

Appendix to Media Release 28 November 2013/ Claims for damage in asphalt cartel matter 3

Kemijärvi - Lemminkäinen Oyj - Skanska Asfaltti Oy	**104.446,96 euro** - joint and several liability	**21.974,28 euro** -Skanska Asfaltti Oy Claim against Lemminkäinen Oyj is dismissed.	**15,00%**	**152.000 euro** -Skanska Asfaltti Oy **22.351,66 euro** -Kemijärvi pays Lemminkäinen Oyj
Kerava - Skanska Asfaltti Oy	**901.582,06 euro**	**211.068,40 euro**	**15,00%**	**90.000 euro**
Kiiminki - Lemminkäinen Oyj	**241.059 euro**	**130.091,60 euro**	**15,00%**	
Kouvola - Lemminkäinen Oyj	**964.205,12 euro**	**674.204,98 euro**	**15,00%**	**42.000 euro**
Kuhmo - Lemminkäinen Oyj	**215.635,00 euro**	**88.482,70 euro**	**15,00%**	**162.000 euro**
Kuopio - Lemminkäinen Oyj	**3.413.605,80 euro**	**877.102,69 euro**	**15,00%**	**126.000 euro**
Lappeenranta - Lemminkäinen Oyj	**416.460 euro**	**416.460 euro**	**15,00%**	**40.000 euro**
Lieksa - Lemminkäinen Oyj	**114.875 euro**	**57.438,56 euro**	**15,00%**	**32.000 euro**
Mikkeli - Lemminkäinen Oyj	**1.209.189,89 euro**	**604.547,56 euro**	**15,00%**	**207.000 euro**

Appendix 1d

Appendix to Media Release 28 November 2013/ Claims for damage in asphalt cartel matter 4

Naantali - Lemminkäinen Oyj	**491.296,33 euro**	**327.530,91 euro**	**20,00%**	**125.000 euro**
Nivala - Lemminkäinen Oyj	**152.896,32 euro**	**76.448,18 euro**	**15,00%**	**195.000 euro**
Nurmijärvi - Skanska Asfaltti Oy - NCC Roads Oy	**664.594,90 euro** - joint and several liability in part	**100.734 euro** - joint and several liability in part	**15,00%**	**133.000 euro** - joint and several liability in part
Oulu -Lemminkäinen Oyj	**3.365.594 euro**	**1.849.227,83 euro**	**15,00%**	**68.000 euro**
Paimio -Lemminkäinen Oyj	**273.811 euro**	**182.540,40 euro**	**20,00%**	**175.000 euro**
Pori -Lemminkäinen Oyj	**869.331 euro**	**681.091,26 euro**	**15,00%**	**111.000 euro**
Raasepori -Lemminkäinen Oyj	**762.435,01 euro**	**65.243,51 euro**	**15,00%**	**60.000 euro**
Raisio -Lemminkäinen Oyj -VLT Trading Oy estate in bankruptcy	**921.553 euro** - joint and several liability	**326.397,08 euro** - joint and several liability **399.381,25 euro** - VLT Trading Oy	**15,00%**	**100.000 euro** - joint and several liability in part

Appendix 1e

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Rovaniemi -Lemminkäinen Oyj -Skanska Asfaltti Oy	**2.666.789,98 euro** - joint and several liability	**479.800,67 euro** - joint and several liability **197.267,34 euro** - Skanska Asfaltti Oy	**15,00%**	**230.000 euro** - joint and several liability in part
Salo -Lemminkäinen Oyj	**1.510.747,70 euro**	**1.3467433.70 euro**	**15,00%**	**132.000 euro**
Siilinjärvi - Lemminkäinen Oyj - Skanska Asfaltti Oy -VLT Trading Oy estate in bankruptcy	**518.543,18 euro** - joint and several liability	**5.816,14 euro** - Lemminkäinen Oyj **32.755,12 euro** - VLT Trading Oy **138.111,14 euro** - Skanska Asfaltti Oy	**15,00%**	**100.000 euro** - joint and several liability in part
Sodankylä -Lemminkäinen Oyj -Skanska Asfaltti Oy -SA-Capital Oy	**51.467,07 euro** - joint and several liability	**21.171,15 euro** - Lemminkäinen Oyj and Skanska Asfaltti Oy joint and several liability	**15,00%**	**226.000 euro** - Lemminkäinen Oyj and Skanska Asfaltti Oy joint and several liability **53.496,42 euro** -Sodankylä pays SA-Capital Oy
Suomussalmi -Lemminkäinen Oyj -SA-Capital Oy	**299.135,28 euro** - joint and several liability in part	**87.870,01 euro** -Lemminkäinen Oyj Claim against SA-Capital Oy is dismissed.	**15,00%**	**140.000 euro** -Lemminkäinen Oyj **48.841,82 euro** -Suomussalmi pays SA-Capital Oy

Appendix 1f

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Tampere -Lemminkäinen Oyj	**4.607.798,57 euro**	**2.974.076,82 euro**	**20,00%**	**175.000 euro**
Turku - Lemminkäinen Oyj -VLT Trading Oy estate in bankruptcy	**5.862.541,30 euro** - joint and several liability	**2.230.359,11 euro** - VLT Trading Oy **2.744.460,34 euro** - joint and several liability	**15,00%**	**122.000 euro** - joint and several liability in part
Tuusula -Lemminkäinen Oyj	**1.169.780,35 euro**	**588.164,36 euro**	**15,00%**	**132.000 euro**
Vantaa - Lemminkäinen Oyj - Skanska Asfaltti Oy -VLT Trading Oy estate in bankruptcy - NCC Roads Oy - SA-Capital Oy - Rudus Asfaltti Oy - Super Asfaltti Oy	**5.111.862,05 euro** - joint and several liability in part	**3.807.092,55 euro** - joint and several liability in part	**20,00%**	**310.000 euro** - joint and several liability in part
Äänekoski -Lemminkäinen Oyj	**145.683,13 euro**	**70.445,85 euro**	**15,00%**	**33.000 euro**
In total	**65.992.598,31 euro**	**37.449.400,92 euro**		**5.797.144,20 euro**

Appendix 1g

Appendix to Media Release 28 November 2013/ Claims for damage in asphalt cartel matter 7

Plaintiff - Defendants	**Capital Claim**	**Capital Sum Awar-ded**	**Percenta-ge Over-charged**	**Legal Costs**
The State of Finland - Lemminkäinen Oyj - Skanska Asfaltti Oy -VLT Trading Oy:n estate in bankruptcy - NCC Roads Oy - Interasfaltti - SA-Capital Oy - Rudus Asfaltti Oy - Super Asfaltti Oy	**56.683.523,04 euro**	Case is dismissed.	-----	The State of Finland pays: **1.295.443,80 euro** - to Lemminkäinen Oyj **17.175,94 euro** - to VLT Trading Oy:n konkurssipesä **480.599,53 euro** - to Skanska Asfaltti Oy **69.822,81 euro** - to SA-Capital Oy **218.435,47 euro** - to NCC Roads Oy **218.435,47 euro** - to Interasfaltti Oy **273.835,84 euro** - to Rudus Asfaltti Oy **25.674,62 euro** - to Superasfaltti Oy **Total** **2.599.423,48 euro**

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Injecting Competition in Broadcasting through MCMO Regulations: Some Recommendations for Mexico

Alexander Elbittar (CIDE), Ernesto Flores-Roux (CIDE), Elisa Mariscal, (CIDE & Global Economics Group)
&
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Injecting Competition in Broadcasting through MCMO Regulations: Some Recommendations for Mexico

Alexander Elbittar, Ernesto Flores-Roux, Elisa Mariscal, & Martin Cave[1]

I. INTRODUCTION

The new telecommunications regulator in Mexico, Instituto Federal de Telecomunicaciones ("IFT"), recently issued a public consultation on its draft regulation for must carry and must offer ("MCMO") conditions in the broadcasting sector. This, together with the recent Constitutional reforms on Telecommunications and Broadcasting, represents an unprecedented opportunity to instill the sector with much needed competition.[2]

For instance, in broadcasting, free-to-air ("FTA") TV is dominated by two main operators, Televisa and TV Azteca, each holding approximately 65 and 25 percent audience share, respectively. Both enjoy also a high level of concentration in infrastructure, audience, and publicity. Something similar occurs in telecommunications, where there is a high level of concentration: Telmex, the incumbent fixed-line operator, has close to 80 percent share of the fixed-line market, and Telcel, the incumbent's mobile affiliate, accounts for almost 70 percent of mobile subscribers.

The new regulatory effort in Mexico's telecom sector also allows for a comparison of the current state of regulation relative to other economies. We take the cases of Argentina, Australia, Brazil, Canada, Chile, the European Union (Ireland and the United Kingdom), India, Peru, and the United States, as illustrative of the different factors that lead to the decision to design and apply MCMO regulation.

This article proceeds as follows. We begin with a brief review of the need to regulate the telecom and broadcasting sector and discuss the circumstances that lead to regulation. Next, we summarize the main issues that the IFT is seeking to clarify, based on the Constitutional amendment of last June 2013, through secondary regulation and its likely effects in the sector. Among those effects is a requirement to protect the audience's right to programming content, while preserving and promoting competition in various broadcasting outlets. Although not

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[2] *See* OECD (2012), *OECD Review of Telecommunication Policy and Regulation in Mexico*, OECD Publishing. Available in: http://www.oecd.org/sti/broadband/49536828.pdf

specifically stated, these rights also include the rights of advertisers to have access to local audiences and the need to continue copyright protection.

Next, we review similar regulation in different economies and derive common elements and mechanisms used by different agencies to pursue regulatory objectives in broadcasting. We conclude with an attempt at deriving best practices in the application and enforcement of MCMO regulation worldwide that may be useful to consider in Mexico.

II. MCMO REGULATION

A. General Characteristics of Telecommunications and Broadcasting

The telecommunications and broadcasting sectors are characterized by a service activity in which economies of scale in production and network externalities in demand prevail, leading to high fixed infrastructure costs. On the supply side, these features lead to a reduced number of operators, with strong incentives for these operators to vertically integrate.

On the demand side, users tend to benefit from having other users consume these goods and services, which in turn leads all users to increase their consumption of goods or services—that is direct network externalities exist. In addition, there is evidence that individuals show persistence in their consumption patterns, even where entry has occurred in different broadcasting markets; it may be too soon, however, to determine whether this preference for legacy broadcasters continues.

An additional feature of broadcasting markets relevant to this discussion is that they operate as a multi-sided platform. Markets characterized as multi-sided platforms serve two or more groups of interdependent users who obtain mutual benefits by jointly participating in the platform. In other words, the demands of different user groups are strongly interrelated in an environment of network externalities in consumption.

Products and services in this sector are subject to fast technological innovation, which has opened potential niches for competition amid an environment of digital convergence. Today generators and transmitters of digital signals and content compete in the telecommunications market, either through FTA broadcasting, restricted or paid broadcasting (cable and satellite), mobile telephony, landline, or the internet.

B. Regulatory Objectives in Broadcasting

Modern regulatory agencies have tried to regulate this market through simple, clear, and transparent regulatory principles that promote interconnection between different networks, and foster technological convergence and competition among them in different marketing channels. More recently, in response to concerns of plurality, regulatory objectives also reflect these concerns, as they now consider relevant both that a diversity of viewpoints exist, and preventing the concentration of influence with only one media owner.[3] General principles that guide regulatory action include: clarity, transparency, network interconnectivity, technological convergence, competition, and plurality to promote efficiency and economic welfare.

[3] Definition taken from Ofcom, Measuring Media Plurality, June 2012.

Following the logic of a multi-sided market platform that characterizes the sector, the ultimate goal of regulation in telecommunications and broadcasting is, on the one hand, to allow audiences access to a sufficient variety of service options that meets their preferences within a competitive environment in terms of variety, price, and quality. On the other, regulation seeks to facilitate different generators of content and their advertisers—the money-making side of this platform—to provide information and entertainment services to their desired audiences.

Thus, a clear policy objective is to raise the economic and social welfare of the different user groups involved in the market (i.e., audiences, generators, and transmitters of content and advertisers) and to guarantee the rights of audiences—in the case of Mexico, this is defined as allowing "[…] free access to plural and timely information and to seek, receive and impart ideas of any kind through any means of expression." (Article 6 of the Mexican Constitution).

In the specific case of broadcast television, audiences are interested in enjoying programming with relevant information and entertainment value for them, while advertisers are willing to pay to get their messages to potential consumer groups. FTA operators are then interested in capturing as large an audience as possible to attract airtime purchases from local and national advertisers.

In the case of pay television networks, subscribers are interested in seeing programming that is popular (i.e. consistent with their preferences such that they derive some degree of “utility” from viewership), local (in the sense that content is relevant to the environment in which the audience and advertisers converge and operate), with the greatest variety and best viable transmission quality available. Subscribers may be willing to pay for access to a platform that gives them these services, so that in contrast to the FTA TV model, the Pay TV providers receive additional income from subscribers.

On the one hand, FTA and Pay TV operators compete for audiences and for local and national advertisers who may see their airtime as complementary and/or substitutable. On the other hand, there is a vertical relationship between Pay TV and FTA operators as Pay TV operators offer an additional distribution outlet for content by FTA operators, who are able to reach a selected group of viewers who would not view the FTA´s content if this were not shown over a paid TV platform. In addition, FTA broadcasters are able to extend their network by offering their signal through Pay TV operators to better exploit network externalities. Pay TV operators also benefit from FTA content as it increases the variety of content available to their users.

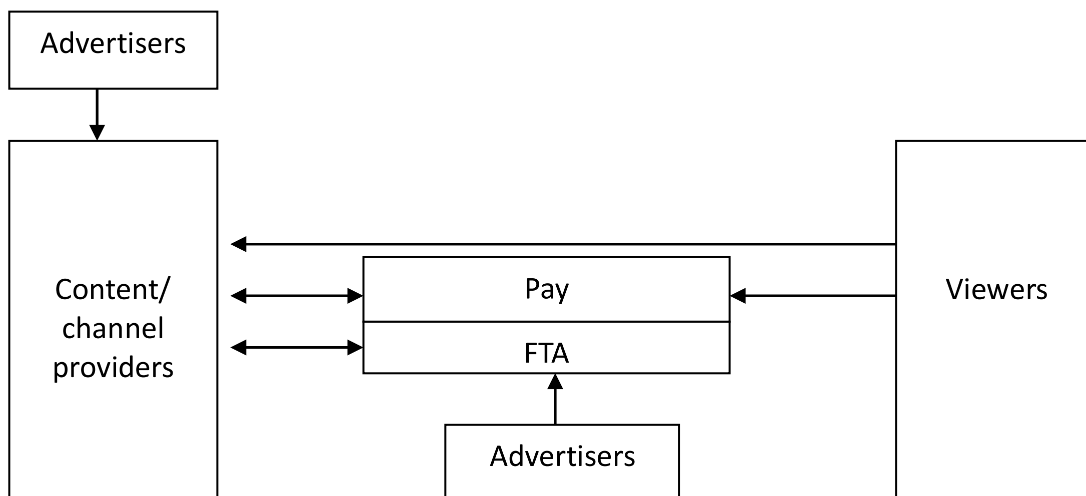
C. The Goals of Must Carry and Must Offer Regulation

Any regulation aiming to establish must carry and must offer conditions must take into account the interaction among the different players in the broadcasting value chain: content generators, transmitters, wholesale programmers, channel schedulers, retail TV (FTA and Pay TV operators—cable, satellite, and possibly streaming), as well as local and national advertisers. In addition, it must consider the multi-sided nature of this market. In the absence of a careful analysis, broadcasters may have incentives to relay signals that will provide the highest profit without regard to the specific needs of the audience or advertisers who are ultimately the consumers in this two-sided market.

Must carry/must offer rules are regulatory interventions that require justification. Here we address the justification question, adopting the conventional approach of evaluating the outcome in the absence of intervention and assessing whether there would be adverse effects without it, either through market failure or through other consequences such as loss of plurality or universal service.

The commercial context is illustrated in Figure 1. Content or channel providers generate revenues from some combination of advertisers, broadcasters, and (particularly in the case of over the top ("OTT") services) directly from viewers. Pay TV operators generate revenues from viewers. FTA broadcasters generate revenues from advertisers, and both of these receive revenues or make payments to content providers. Viewers pay for the experience either in monetary terms or by making their eyeballs available to watch advertisements. It is important to recognize that broadcasters often make their own content: vertical integration of this kind is an important feature of the situation.

Figure 1



The monetary flows in broadcasting as a whole provide the wider context, but our immediate focus is on flows between content providers and broadcasters/platform providers. We observe that, absent regulation, such flows can—in net terms—go in either direction. In some cases a broadcaster will pay for content to be available for distribution on its platform; this will occur if the content is unique and seen as attracting viewers to the broadcaster. In other cases a content provider offering one of a number of substitutable "basic" channels may have to pay for distribution. The direction of flow depends essentially on the balance of advantage between the two sides of the bargain.

At any moment physical constraints on carriage capacity limit what can be carried by each broadcaster and on each major platform (cable, Digital Terrestrial Television (DTT), etc.). While these constraints have clearly loosened since the days when the broadcasting sector consisted of a handful of analogue terrestrial channels, the vast expansion of carriage capacity in recent decades has been matched by an equally vast proliferation of content.

Why not in these circumstances just accept the outcome that market forces produce? Here we answer this question not in terms of the struggle between the commercial forces favoring or disfavoring particular forms of regulation, but in terms of possible adverse effects on viewers in a market free-for-all. These effects fall broadly into three categories:

Abuse of market power: Some premium content confers market power on its owner or acquirer, because of its irreproducibility; thus there can by definition be only one 'best' soccer league in any country. The holder of such rights, if vertically integrated into broadcasting, can leverage its market power into other components of the value chain, including the retail Pay TV market. This is the origin of much must-offer regulation, which requires owners of certain program rights to make them available to multiple broadcasters and platforms.[4] If the FTA broadcasting market is highly concentrated, a must-offer obligation may be imposed requiring popular FTA programming to be made available on nascent pay channels, for example.

Wider access to public service broadcasting services: Public service broadcasting content typically reflects both positive and negative programming requirements, which require, respectively, the inclusion of certain types of programming (say, children's or cultural programming) and the exclusion of other types of programming (say, violent programming). It is consistent with the logic of the intervention that such programming be made available to as wide an audience as possible. Hence must-carry obligations for certain types of FTA programming are imposed on pay platforms in many countries.

Localism: It is desirable that in the interests of pluralism, viewers have access to local programs dealing with important issues in their own communities, as well as national programs which are usually more commercially supportable. For this reason, pay broadcasters are often required to retransmit local channels (a must-carry obligation).

As with most access questions, must-carry/must-offer regulation involves two questions: the scope of mandated access and the terms and conditions on which it is made available. With limited carriage capacity, some form of rationing is often required. With must offer, price regulation is usually required, the usual alternatives of *cost–based pricing* and *retail minus* being the usual candidates. *Carriage prices* are also relevant for must-carry obligations. Since FTA broadcasts are normally advertiser-financed, and since must carry increases viewers, the question of attribution of the enhanced advertising revenue comes into play.

III. PROPOSED REGULATION OF MCMO CONDITIONS IN MEXICO

A. Mexico's Proposed Regulation

The Mexican government is currently attempting to ground in secondary legislation some of the general principles included in the Constitutional reform of last June 2013 concerning must-offer and must-carry conditions. One of the transitory articles of the decree (the eighth) requires FTA TV licensees to offer their television signals to Pay TV licensees (i.e. must-offer obligations).

[4] *See* M. Cave & P. Crowther, *Regulating access to content in the European Union*, (4) J. LAW & ECON. REG. pp. 133-150 (2011).

This article also includes must-carry obligations as Pay TV licensees must retransmit FTA TV signals. In both cases, the Constitution decrees, the signals offered and their retransmission must be "[...] free of charge and without discrimination, within the same geographic coverage area so, complete, simultaneous and without changes, including advertisements, and with the same signal quality that is broadcast [...]."

In a sense, the Constitutional mandate overrides any questions regarding the terms and conditions upon which content is made available, which we mentioned previously. This represents a challenge in its implementation as it specifically protects rights of audiences but omits to mention the two-sided nature of the market and any copyright issue that may arise with retransmission among different platforms (FTA and Pay TV) or regions (national, regional, local-to-local). It does, however, leave open for further clarification in regulation the question of the scope of mandated access—a key focus of the IFT in its draft regulations.

Must-carry and must-offer conditions in the Constitution distinguish three types of broadcasters: those who provide FTA television broadcasting, those who provide Pay TV service, and those who provide satellite Pay TV services. These broadcasters have the right—not the obligation—to retransmit any broadcasted signal within their area of coverage, but they have the obligation to retransmit public service broadcasts at a federal level.

The distinction among pay TV broadcasters is relevant because satellite providers are exempted from carrying all must-offer content and are only required to carry FTA channels with coverage of more than 50 percent of the national territory. Only those telecommunications and broadcasters who have been declared "with substantial market power" in any of the telecommunications and broadcasted markets will have to pay for this FTA signal. These economic agents are barred from passing on the additional costs of the service to their subscribers or users.

B. Some Shortcomings of the Proposed Guidelines Relative to the MCMO Reform

The phrasing in the Constitutional text leaves open several interpretations for the must offer rule on FTA broadcasters as it pertains to satellite providers. First, is the determination of the 50 percent national coverage rule, which the guidelines attempt to clarify by defining concepts such as transmission channels, relevant audience, territorial coverage, national chains and commercial brands, similar programming, etc. But there are other concepts and methodologies that the guidelines do not clarify and in some cases do not address.

As we have noted before, the purpose of regulation in this market is to ensure that services meet preferences for two main groups of consumers: audiences and advertisers. The Constitutional decree considered these groups, particularly the first group, to be so important as to define the rights of audiences as a human right. Audiences, similarly to citizens, are rarely homogeneous and their needs and preference have to be ascertained at a local level. Nonetheless, the proposed guidelines leave out precisely those human rights considerations, in favor of proposing a rule that will enable operators to carry four "standardized" signals over a national territory that includes more than 100 million diverse viewers and advertisers.

In more specific terms, territorial coverage at a geographic/territorial level ignores the nature of the programming consumption that is local/city-wide/municipal in nature. Given the

nature of telecommunications markets, both audiences and advertisers would be interested in sending and receiving information at a local level. Welfare is maximized the greater the specificity of service that consumers aspire to.

This degree of specificity is very important in four aspects: political messages and campaigns, local advertising and events, local news, and emergency alerts. A serious shortcoming of the current proposal can be gleaned in the political arena whereby a local politician could quickly become a national figure simply by appearing in national territory in one of the four "standardized" signals that cannot be modified.

On the other hand, rating programming content of the different signals based on their similarity, and not on local demand for content, ignores consumer preferences in specific localities/cities/ municipalities. The audience in Mexico City, for example, will hardly have an interest in local news and advertisements in border cities and vice versa.

Finally, there is no consideration about the two-sided nature of the market. The rights of advertisers to reach certain audiences, for example, are completely ignored.

Some key questions that do not appear to be addressed are: What was the original market failure that made this regulation necessary? Where is the problem of potential abuse of dominance in this market? Is it the owner of the signal or of the content or is it the broadcaster? Must-carry and must-offer rules are different in nature and seek to resolve different problems in a preemptive manner: abuse of dominance, widening access to public broadcasts, and fostering localism.

In Mexico, the main competition problem that led to the application by the Competition Commission of this rule is the refusal of generators of content (FTA TV) to sell their signal to Pay TV operators. The ideal mechanism to limit this kind of abuse was a must-offer rule. Nevertheless, although a potential abuse of dominance problem has not been detected among Pay TV operators, it was regarded as important to defend content plurality objectives for audiences as well. At the time, the Competition Commission opted to impose must-carry obligations to ensure that Pay TV operators would carry programming and ads to larger audiences who would benefit from a greater variety of programming (see our discussion of Mexico in the next section).

International experience, however, presents an interesting contrast to the market failure that each country and sectorial regulator has faced in the broadcasting sector. We believe that a review of this experience can better inform the Mexican regulator both in determining what its policy objectives are, its priorities in attaining these objectives, and in elaborating further on its proposed guidelines for MCMO regulation. We turn to these international examples next.

IV. INTERNATIONAL EXPERIENCES IN MCMO REGULATION

Broadly speaking, most countries have tried to ensure that Pay TV subscribers have access to free-to-air broadcasting transmissions. Depending on the particular situation of each market, countries can be separated into three broad categories, though this clustering is by no means clear-cut, as two defining issues tend to be tackled simultaneously:

a) The first group is formed by countries where market forces have—with very little intervention—reasonably solved the problem, and FTA broadcasts are available to all Pay TV subscribers.

b) A second group is defined by situations where broadcasters are in a better negotiating position than Pay TV carriers and, thus, regulation focuses more on must-offer obligations.

c) Finally, a third category is formed by countries where the reverse is true, so regulation addresses must-carry obligations (e.g., the United States). We briefly address some case studies that illustrate these different regulatory approaches.

A. Argentina

Current regulation in Argentina for broadcasting services is Ley Nº 26.522, enacted on October 10th 2009. Before the present law broadcasting services were regulated by Ley Nº 22.285, enacted by the *de facto* government in 1980.

The new law was developed to update democratic needs, as set forth by the current government. There were several interesting points, commonly referred to as "the 21 points," that established that broadcasting cannot be managed only as a commercial business and that it needs to be independent from pressures, both public and private.

There are no specific must-carry / must-offer regulations in the new law, but in Articles 21 and 65, there are specific references to the "Joint Declaration on Diversity in Broadcasting" of December 2007. Among them, "[…] specific measures to promote diversity may include reservation of adequate frequencies for different types of broadcasters, must-carry rules, a requirement that both distribution and reception technologies are complementary and/or interoperable, including across national frontiers, and non-discriminatory access to support services, such as electronic program guides." This, in essence, allows the establishment of must-carry / must-offer rules to be imposed at the regulators' will (Autoridad Federal de Servicios de Comunicación Audiovisual, AFSCA).

Some of these must-carry obligations refer to the retransmission of specific content, such as national or local content, educational content or public channels, and others refer to the retransmission of FTA channels. In Article 65, it is stated that stationary reception subscription television services shall include unencoded broadcasts and signals generated by Radio Television Argentina Sociedad del Estado, all public broadcasters and signals of the National State, and those in which the National State has an interest. Additionally, non-satellite subscription television services shall include at least one signal of own local production that satisfies the same requirements as for FTA television broadcasts.

Moreover, in the same Article there is an obligation for broadcasters owned by Provincial Governments, Buenos Aires City Government, municipalities, and national universities that they shall broadcast educational, cultural, or public interest programs equivalent to at least twenty percent of total program contents. This obligation, however, is not enforceable with private and non-state broadcasters. Also, there are specifications regarding national content. The same article states that audio broadcasters shall broadcast at least 70 percent of national production, while FTA television broadcaster shall broadcast at least 60 percent of national production.

On the other hand, other must-carry specifications refer to the retransmission of FTA channels. For instance, in Article 65 it is stated that non-satellite subscription television services shall include unencoded signals generated by the originating FTA television services with the same coverage as their service area.

B. Australia

As in the United States, most issues related to must carry/must offer are addressed in copyright legislation. The Copyright Act of 1968 states that the maker of a television broadcast is the owner of any copyright subsisting in the broadcast (Division 5, Subdivision A, 99). The same act provides a statutory licensing scheme for re-transmission of an FTA broadcast, as long as written notice is provided and remuneration is paid to the relevant collecting society. Re-transmission, as defined in the Broadcasting Services Act ("BSA"), refers to the re-transmission of a broadcast, provided it is unaltered and either simultaneous with the original transmission or delayed until no later than the equivalent local time. Even though the act states that no "action, suit or proceeding lies against a person" that re-transmits content, this only applies to either national broadcasters or local broadcasters within the licensing area; it does not apply to re-transmissions of local content outside the licensing area, unless a permit is granted by the Australian Communications and Media Authority ("ACMA"). The re-transmissions, as specified, are not exempt from copyright rules, as set forth in the Copyright Act (Section 212 of BSA). Several exemptions are outlined for "self-help providers," which, in essence, re-transmit content for the sole or principal purpose of obtaining or improving reception.

Pay TV in Australia has not made significant inroads. Pay TV penetration is at just 29.2 percent of households (2012, latest official figure available). Ratings, as published by Oztam,[5] which is the recognized official source of television audience measurement, are estimated at 84.8 and 15.2 for FTA and Pay TV, respectively (as of week 5 of 2014); these ratings have remained stable since 2008. Even for Pay TV subscribers, FTA channels reach ratings of 56.2.

The Pay TV sector is dominated by Foxtel, which is a 50/50 joint venture between Telstra (the incumbent telecommunications provider) and NewsCorp (Fox), with a market share of over 90 percent (2.55 million subscribers). A significant part of Foxtel's share came from various acquisitions through time. It provides cable, fiber, and satellite Pay TV; satellite is only offered where it cannot offer fiber television services.

The unimpressive development of the Pay TV industry is a direct consequence of the quality and diversity of the offer of FTA channels (currently 16), as well as "anti-siphoning" legislation, set forth in the BSA. These rules prevent Pay TV providers from acquiring rights to televise certain listed events (for example, the Olympic Games, and certain Australian Rules football and cricket matches) unless certain conditions are met. Pay TV providers can only acquire the rights to transmit after FTA broadcasters pass on these events.

Anti-siphoning legislation was introduced in 1994 to ensure that television coverage of events of national importance and cultural significance were not siphoned off exclusively to

[5] www.oztam.com.au, an independent company owned by Australia's major commercial television broadcasters (the Seven Network, Nine Network and Network Ten) and has an independent, non-executive chairman

subscription TV subscribers. Currently, it covers 1,100 events, excluding the Olympics. These rules were reviewed in 2009, creating a two-tier list of events subject to anti-siphoning rules, allowing the minister to specify certain quotas, and restricting new platforms (e.g., IPTV) from acquiring exclusive rights of anti-siphoning events. The Australian Government recognizes that the anti-siphoning scheme creates commercial benefits for the FTA broadcasters at the expense of other platforms, but in its Convergence Review of March 2012[6], it stated that, given that the proposed changes were still before Parliament, it believed that it was not appropriate to recommend further changes. These recommendations have not yet been through the Legislature.

C. Brazil

In Brazil, must-carry rules are part of the current regulation of the broadcasting industry. Prior to the 90s, state participation in TV was quite limited, and occurred mainly through the creation of educational broadcasting companies. Apart from isolated initiatives, institutional forms that ensured media access were implemented only in the 1990's, through two main mechanisms: (i) community radio broadcasting and (ii) participation in community and university cable TV channels.

Community radio broadcasting was legally regulated in 1998, defining community radios as low power and limited-reach broadcasting stations directed by foundations and by non-profit community associations.

Community and university television channels are, as a result of the Cable TV Law (1995), obligatorily transmitted by Cable TV providers. This law—a remarkable exception in Brazilian legislation—was enacted as a result of a rich interaction between organized civil society groups, market, and governmental representatives. The outcome was an innovative law that imposed must-carry regulations, including new "public" channels (such as university and community channels), which should be carried on cable service provider's system.[7] Even so, the low penetration of the service and problems associated with the shared use of these channels still represent obstacles to the right to communicate.

Every Pay TV operator has the obligation of transmitting public legislative channels from municipalities, estates, and from the Federation.

Regarding private channels, Pay TV operators have the obligation of transmitting all channels available in their coverage areas, in format UHF or VHF. Additionally, they must transmit channels from universities, educational-cultural channels, community channels, and channels from non-profit non-government organizations.

As regards to specific content obligations, Pay TV operators should include at least one channel that transmits Brazilian cinematograph or broadcasting productions.

Until recently, Brazil had regulated Pay TV services depending on the technological platform: cable, MMDS, and satellite. As all telecommunications platforms started converging, this type of regulation became obsolete. It was recognized around 2005 that a new regime for

[6] Australian Government, Department of Broadband, Communications and the Digital Economy, *Convergence Review* (March 2012).

[7] Must-carry rules are not applicable to MMDS and to DTH, other Pay TV platforms.

audiovisual services was necessary, but the discussion quickly became political, as many different parties raised a large number of issues. Among them, legislators, as well as the executive branch, wanted to promote the development of local content; the discussion of this matter got entangled into restrictions, protectionist measures, and subsidies.

Another crucial issue was the foreign ownership restriction that existed on Pay TV carriers. At the beginning of the decade, Telmex (now America Movil) had bought a minority stake in Net—a subsidiary of Globo providing cable TV services—that was in financial difficulty. Net's acquisition was relevant, as it allowed Embratel, the long distance incumbent that was also controlled by Telmex, to get into the wireline last-mile market. Lifting the ownership restriction would allow Telmex to increase its stake, make bundled offers, and realize synergies and, thus, increase competition; most telecommunications service providers, realizing this fact, adamantly opposed this change.

Lastly, not all platforms were carrying all the local channels; the selection of channels was somewhat arbitrary and, in a way, discriminatory. It was deemed necessary by the government and legislators that most signals were to be made available to Pay TV customers.

After several years of discussions, Congress approved the Conditional Access Service Law ("SEAC") in 2011;[8] a few months later, Anatel, the regulator, published the regulations to complement the law.

These regulations clearly impose must-carry obligations for local-into-local transmissions, independently of the technological platform used. This was somewhat onerous to MMDS players, but these platforms have become obsolete and have mostly disappeared, especially after the acquisition of TVA (Televisão Abril) by Telefónica in 2006, which was deemed valuable because of its spectrum holdings (in certain places, 190 MHz in the 2.5 GHz band).

The new legislation allows telecom providers to offer Pay TV. New licenses, which were auctioned in the past, are now offered for only R$ 9,000 (around U.S. $4,000), with no restrictions on the technological platform; they are valid nationally, as opposed to a predetermined local area. Minimum size is not imposed; so, at least theoretically, any given company can provide services only locally (e.g., a neighborhood) or cherry pick subscribers in a larger area.

A very controversial issue is the obligation to carry local content: 3.5 hours per week on prime time (18-22 hours). For bundles, at least a third of the channels must be Brazilian; half of this quota has to be developed by independent producers not linked to broadcasting groups.

Cable and other fiber operators have had no trouble adjusting to the new legislation, offering all FTA channels on their platform, as well as all the additional must-carry obligations (Congress, educational, etc.). By contrast, satellite operators have had significant trouble complying with the new regulation and have applied for exemptions or extensions, which were contemplated in the law. In July 2013, GVT, a DTH (Direct-to-Home) operator, announced it was missing 9 out 14 FTA channels and started negotiating with Anatel. The main reason for not being able to meet its obligations was the failure of Intelsat 27, which would have given GVT the

[8] Lei 12.485 de 12 setembro 2011, Lei do Serviço de Acesso Condicionado.

capacity required. In October 2013, Sky Brasil, owned by News Corp, also applied for an exemption of the rule, as they did not have the required capacity to carry the more than 500 analogue channels generated in different regions ("local into local," for an operator with national footprint).

D. Canada

All Canadian cable television systems and wireless systems (e.g. MMDS) must provide all of its subscribers a standard package of services consisting of a number of mandatory ("priority") Canadian programming services, including the CBC English and French network services, local and regional stations, and educational services. As for Canadian DTH satellite distributors, they are required to distribute the CBC English and French network services and the programming of at least one affiliate of each national television network licensed on a national basis (e.g. CTV).

In April 1996, the CRTC announced new rules designed to ensure that there was fair and equitable access to television broadcasting services. Under these access rules, cable television systems with 6,000 or more subscribers, as well as DTH satellite distributors and major wireless systems (e.g. MDS), must generally distribute, in addition to priority television signals, all Canadian specialty and pay television services appropriate for their markets, such as those in the predominant official language of that market. These rules will be revised by the CRTC this coming fall.

Foreign satellite services can be distributed on a discretionary basis, in a package with Canadian specialty and/or pay television services. Canadian pay television services can be offered in a package with up to five channels allocated to foreign satellite services. Each Canadian specialty service within a discretionary tier may be linked with no more than one channel allocated to foreign satellite services. These linkage rules are designed to give Canadian cable subscribers access to the most popular foreign services and to ensure the maximum exposure of Canadian specialty services.

E. Chile

In August 2012, Chile made modifications to its treatment of digital terrestrial television, with regards to consensual retransmission to cable operators of content from open television.

With the new regulation, cable operators are able to issue or retransmit signals from FTA channels when their coverage does not exceed 85 percent of the population in a particular region. Once coverage surpasses that percentage, open television channels and cable operators can negotiate some kind of economic compensation.

Must-carry obligations were imposed: cable operators have to incorporate in their programming, when technically possible, at least four local, community, or regional channels.

The intention of the must-carry obligations is to enhance regional broadcasts. In case there are more than four channels, the promotion of education and culture should become the main decision criterion.

F. The European Union

All 28 member states must abide by legislation on must-carry as was initially set out in a 2002 European Union Directive,[9] which was essentially unchanged on revision in 2009. Each Member State can choose how to implement the directive taking into consideration its own conditions. In the case of Belgium, the European Commission has taken enforcement action to ensure that the provisions are implemented properly.

The Directive gave Member States the right to impose reasonable obligations where a significant number of end users of such services used them as their principal means of receiving broadcasts. The obligations should be in the interest of legitimate public policy considerations and should only be imposed where they are necessary to meet clearly defined general interest considerations. Such obligations should be transparent and proportionate.

The years since 2002 have seen a variety of cases before the European and national courts clarifying the nature of the must-carry provisions in relation to cable systems and to IPTV. Surveys of recent or current application of the rules can be found in several publications.[10]

1. Ireland

In Ireland, must-carry and must-offer obligations are regulated in the Broadcasting Act of 2009, in its Article 77, which applies to specific signals or channels. For instance, in subsection (3) it determines that "when the network is a digital system, the appropriate network provider shall ensure the re-transmission, by or through its appropriate network, of the Houses of the Oireachtas Channel and the Irish Film Channel."

Subsection (4) states that "an appropriate network provider shall ensure the re-transmission, by or through his or her appropriate network, of each free-to-air television service provided for the time being by RTÉ, TG4 and the free-to-air service provided under *section 70* by the television service program contractor which that body or contractor requests the appropriate network provider to so re-transmit."

Regarding carriage fees, subsection (7) states that "The appropriate network provider shall not impose a charge or allow a charge to be imposed in relation to the making available to a person of any service referred to in *subsection (3), (4)*, *(5)* or *(6)* if he or she imposes a charge or allows a charge to be imposed on that person in relation to the making available of any other service to that person by means of the appropriate network concerned."

Moreover, regarding must-offer obligations, subsection (11) states that "RTÉ, TG4 and the television service program contractor shall ensure that their must offer services are at all times offered for re-transmission by means of any appropriate network that is available for reception in an intelligible form by members of the public in the whole of or in part of the State." Additionally, subsection (12) states that "RTÉ, TG4 and the television service program contractor

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[9] Directive 2002/22/EC of the European Parliament and the Council of 7 March 2002 on universal service and users' rights relating to electronic communications services (Universal Services Directive) Article 31.

[10] Deirdre Kervin, Must-Carry Rules: Valuable Tool or Sacred Cow, EPRA/2008/06. Andrew Katolo, *Must carry and must offer in Europe*, SCREEN DIGEST (16/12/2011).

shall ensure that their must-offer services are at all times offered for broadcast or re-transmission by means of every satellite television service."

2. United Kingdom

In the United Kingdom, all the main FTA network services have public service broadcasting ("PSB") requirements, including universality obligations, and they only have limited copyright protections. Significant access fees are paid by the main FTA networks to platforms for re-transmission; broadcasters have to meet their own satellite retransmission costs.

While all the main PSB FTA networks in the United Kingdom must comply with a must-offer obligation across all distribution systems, the BSkyB satellite platform has no must-carry obligation and the FTA networks enjoy no copyright protection when being retransmitted by U.K. cable systems.[11]

All PSB networks in the United Kingdom have universality requirements (in exchange of the benefits they receive) and a specific must-offer requirement within their terrestrial licenses. All the PSB networks also have additionally strong incentives to secure carriage on all platforms. For the BBC, acceptance of household license fee funding is underpinned by universal access to the services financed by that mandatory license fee. For commercially funded PSB networks, the loss of effective access to even small proportions of the available audience can harm their unique proposition to advertisers.

On the other hand, cable systems in the United Kingdom do have a must-carry obligation for PSB networks. However, because cable systems have been exempted from copyright-based retransmission payment obligations, certain players, such as Virgin Media, can effectively re-transmit the main PSB networks without being obliged to pay the PSB networks any money. There is no mechanism for the networks to deny the cable systems their signal and demand a charge for providing it. In practice, this has meant that there has never been a need to enforce existing must-carry obligations.

BSkyB has no must-carry obligations in the United Kingdom. As an "open system," the regulations implicitly assume that PSB networks can go directly to DSAT households and receiver dishes without the need to go through the BSkyB set-top box access system if they wish.

G. India

In India, must-carry and must-provide conditions are regulated in The Telecommunications (Broadcasting and Cable Services) Interconnection Regulation of 2004.

This regulation attempts to deal with the high cost involved in the distribution of TV channels if the market is fragmented. To reduce distribution costs, broadcasters and multisystem operators should be free to provide access in the manner they think is beneficial for them. The "must provide" of signals should be seen in the context that each operator shall have the right to obtain the signals on a non-discriminatory basis; but how these are provided—directly or through the designated agent or distributor—is a decision to be taken by the broadcasters and multisystem operators. Thus, the broadcaster or multisystem operator has to ensure that the

[11] The cable TV systems are specifically exempted from copyright obligations in this respect by Section 73 of the copyright, Designs and Patent Act of 1988.

signals are provided either directly or through a particular designated agent, distributor, or any other intermediary. On the other hand, must-carry provisions are not mandatory.

These provisions were still under analysis when it was published the Notification from the Telecom Regulatory Authority of India. Such notification stated that:

> The majority of the broadcasters are in favor of mandating must carry provisions to balance out the 'must provide' clause prescribed in the existing interconnect regulations. They have suggested that the manner of offering network access should be on a non-discriminatory basis and the qualifying conditions may include openness to audit and transparency, non-discriminatory listing of channels and all channels should feature genre-wise in the EPG of MSO. One broadcaster has also suggested that the 'must carry' provisions need not be mandated.[12]

In addition to the question of whether or not to regulate must-carry provisions, the determination of the carriage fee has become a controversial issue. The News Broadcaster Association is of the view that carriage fees should be regulated. They argue that if must-carry is mandated, the question of a carriage fee does not arise. However, the majority of the broadcasters and one association of broadcasters are not in favor of regulating the carriage fee and have suggested that it should be based on the mutual negotiation between the broadcaster and MSO. Some parties have suggested that the parameters to be used could be the subscriber base of the MSO or the number of STB installed. One of the broadcasters suggested that carriage fees should not exceed 10 percent of the subscription fee collected for the channels not covered under the must-carry mandatory clause.

H. Mexico

The need for this type of regulation arises from competition concerns identified in merger reviews by the Competition Commission in two specific cases: (i) the merger between Televisa, the largest FTA broadcaster in the country, and a cable operator in the third largest city in Mexico (Televisa (CVG)/TVI),[13] and (ii) Televisa's purchase of Cablemas, another cable system with presence in the center and southern regions of the country (Televisa (Paxia) and Cablemas).[14]

As a condition to allowing the first merger, notified in 2006, the competition authority imposed the following conditions to offset potential competition problems:

a) Grupo Televisa would have to divest its participation in the restricted audio and television service provided by SKY® in the geographic areas where TVI had a presence. It would also have to use a mechanism that guaranteed the permanence and viability of SKY® as a competitor in those geographic areas.
b) TVI and its stockholders would no longer be able to participate directly or indirectly as partners in the buying club, PCTV.

[12] Notification. Telecom Regulatory Authority of India. April 30th, 2012, pp. 39.
[13] Case number CNT-048-2006.
[14] Case number CNT-018-2007.

c) Grupo Televisa, its subsidiaries and affiliates, would have to supply, in a non-discriminatory manner, all of its FTA signals restricted to any audio and television operator in TVI's geographic area of operation (*must offer*).
d) Grupo Televisa, its subsidiaries and affiliates, including TVI, would have to provide transmission services of any FTA television channels that requested services in the areas where TVI operated (*must carry*).
e) Members of the Board of Directors or any other parties to decisions in the Board of Grupo Televisa, its subsidiaries or affiliates, would not be able to influence Boards of companies that were offering or could potentially offer the service of restricted audio and television (*no Interlocking Directorates condition*).

Conditions that allowed Televisa to purchase Cablemas in 2007, while seeking to address potential competition problems (including Cablemas's preferential access to content) were:

a) Grupo Televisa had to demonstrate that it was following up on cable operators' complaints regarding discriminatory treatment in content sales within 90 days of having received the Commission's decision (*no discrimination*).
b) Grupo Televisa had to make transparent its content offering for cable operators, and make available to the Commission its contract terms for content provision to cable operators (*regulation of contract terms for content*).
c) Cablemas and its stockholders could no longer participate as partners in the buyers club for paid content, PCTV.
d) Grupo Televisa had to agree to must-offer and must-carry conditions and not undertake anticompetitive conducts listed in the resolution (similar to those included in the law). These conditions were limited, however, to the size and transmission mechanisms of the operator requesting the signals.[15]
e) A no interlocking directorates condition was also included.

I. Peru

EGEDA (Entidad de Gestión para los Productores Audiovisualres)[16] is in charge of issuing licenses, establishing rates and tariffs, and regulating re-transmission of FTA signals. In addition, it regulates specific communication and broadcasting shows that are massive and have difficult individual control, such as retransmission acts and communications in open spaces with free access.

On the one hand, tariffs for cable retransmission are set by EGEDA considering the total number of subscribers of each operator. On the other hand, tariffs for retransmission in open spaces with free access are set by EGEDA considering the category and capacity of the site. EGEDA does not differentiate whether the signals are retransmitted voluntarily or under enforcement of federal legislation.

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[15] This condition is generally interpreted as foreseeing the potential entry of a competitor such as Telmex, who would not benefit from the must carry and must offer conditions imposed by the CFC.

[16] http://www.egeda.com.pe/EPe_Licencias.asp.

J. United States of America

In the United States, the issues of the relationship between pay TV operators and broadcasters appeared more than 30 years ago; since then, the Federal Communications Commission ("FCC") and legislators have dedicated important efforts to address them. Initially, pay TV operators refused to carry FTA signals, so legislation has concentrated on must-carry issues. Must-offer is mostly legislated by the Copyright Act (U.S. Code, Title 17), which imposes statutory licensing and establishes the rule for payments to the owners of the copyright. The Telecommunications Act of 1934 and further amendments, including its overhaul in 1996 (U.S. Code, Title 47) impose, with significant restrictions, must –carry provisions.

Section 614 [47 U.S.C. 534] (*Carriage of Local Commercial Television Signals*) of the Telecommunications Act establishes that all local signals (defined as those that have a broadcasting signal in a given area) must be carried by cable TV operators. Some exceptions are allowed when the transmission capacity is limited. As cable TV is now mostly digital, there are no significant capacity issues and these exceptions are of no real relevance. This section also imposes the condition that the pay TV operator cannot receive compensation for its duty to carry the signal. Legislation is based on the principle of "localism," putting local interests ahead of all others. Must-offer rules are addressed in Section 325 [47 U.S.C. 312] (*False Distress Signals; Rebroadcasting; Studios of Foreign Stations*), in compliance with the *Cable Television Consumer Protections and Competitions Act of 1992*.

Section 335 (SEC. 335. [47 U.C.S. 335] *Direct Broadcast Satellite Service*) mandates that specific rules have to be written for satellite TV providers. These rules have been reviewed periodically (*Satellite Home Viewer Act of 1988*, *Satellite Home Viewer Improvement of 1999* ("SHVIA"), *Satellite Home Viewer Extension and Reauthorization Act of 2004* ("SHVERA") y *Satellite Television Extension and Localism Act of 2010* ("STELA")); all of them have suffered minor changes through their lifetime.

The *Satellite Home Viewer Act* of 1999 allowed satellite TV operators to carry FTA signals only to those consumers who could not receive the FTA signal through an antenna and who were not subscribed to a cable TV service that carried them. This was modified by the SHVIA in 1999, which allowed, but not mandated, satellite TV operators to transport local signals. Consumers could only receive their local signal, not those destined to other local areas; for example, a consumer in New York could receive any of the signals of the four FTA providers (ABC, NBC, CBS, and FOX) that aired in the city, but they could not receive the signal from any other area. This is the concept of "local-into-local." Local areas, 210 in total, are labeled as "Designated Market Areas" (DMAs) and are defined by Nielsen media Research.

The Act also established that signal owners have the right to receive payment and the satellite provider could charge customers for providing service. Additionally, starting in 2002, a satellite TV provider that had decided to retransmit a given signal had to carry all the FTA signals within a given DMA that requested such service. This rule is known as "carry-one, carry-all." The only way of receiving the signal from another DMA ("distant-into-local") was for those households that were classified as "unserved," (certain exceptions were allowed during the transition period). By the end of 2000, the two main satellite TV providers had announced that

they would be providing these services in DMAs covering over 50 percent of the population. By the end of 2005, one of them provided "local-into-local" service in 133 DMAs; the other carrier covered 160.

The SHVERA of 2004, added the possibility of receiving, through the satellite platform, non-local FTA signals if these were considered "significantly viewed" in a given community,[17] and also incorporated provisions for the transition to digital television. With few exceptions, the rules did not allow for "distant-into-local" transmissions.

In 2006, still under SHVERA legislation, the Eleventh Circuit of the Florida Middle District Court banned Dish (originally Echostar) of retransmitting distant signals, after constant and deliberate violations of Section 119 [U.S.C. 17] of the Copyright Act. Echostar had been retransmitting New York and Los Angeles signals to thousands of households that were being served by local broadcasters. On appeal, the Eleventh Circuit of Appeals confirmed the decision; Dish was found to have engaged in such practice by improperly transmitting local signals to ineligible households. It was enjoined from providing distant-into-local transmissions, including "unserved households."

This enjoinment was modified by the STELA Act in 2010, which updated these rules and extended the validity of licenses covered by Section 119 of the Copyright Act for an additional five years. A significant part of STELA is dedicated to rules for multiplexing, as the market had fully transitioned to digital TV. All payments from pay TV providers to broadcasters were updated, including a glide path for the following five years (ending in 2014). For satellite TV, the 2010 monthly fee would be 25 and 50 cents per residential and commercial subscriber, respectively, with annual increases linked to inflation. The definitions of "local area service" and "unserved household" were marginally modified.

Dish reacted positively to STELA's enactment,[18] as the new regulations allowed it to offer FTA signals. The restriction enforced by the Eleventh Court would be lifted when it could offer "local-into-local" services in all 210 DMAs. Dish started the process in June 2010[19] and completed the transition soon thereafter.

Chapter 1, Sections 111, 110, and 122 of the Copyright Act (Title 17) cover the rules for must-offer. Section 111 addresses retransmission by cable TV providers, Section 119 establishes the rules for transmitting distant signals ("distant television"), and Section 122 sets the rules for satellite providers.

Broadly speaking, the rules impose must-offer obligations, with certain restrictions, to all platforms through statutory licensing. The owners of the signals have the right to receive payment, subject to prices and conditions determined by regulation, though in principle they could be negotiated.

Section 111 lists the exceptions to copyright violations when the retransmission is carried by a cable TV provider. It explicitly prohibits carriers from modifying the signals. It also sets the

[17] A complete list can be found in http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-05-187A2.doc.

[18] *See* press release in http://about.dish.com/press-release/corporate/dish-network-statement-passage-satellite-television-extension-and-localism-a.

[19] http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-10-1036A1.doc.

fee to be paid to the owner of the signal as a function of the carrier's gross revenues paid by subscribers. It also restricts the must-carry concept to the local area where the signal is broadcast; that is, a given signal cannot appeal and ask to be carried outside its local area.

Section 119 addresses "statutory licensing" conditions for "distant-into-local" transmissions by satellite TV operators. For network stations, which are defined as the signals with national presence (currently, ABC, CBS, FOX, and NBC), such licensing exists as long as the operator complies with FCC rules and subscribers are charged, either directly or indirectly, for the retransmission. Additional rules apply to unserved households, as well as rules for automatic licensing of local-into-local service.

The sections explicitly ban the retransmission of signals by satellite providers to consumers that do not have the right to receive it; this refers to the transmission of distant signals. Section 119 (a)(6)(B) imposes a total ban of retransmission of local signals to any company that violates this clause. In all cases, fees for retransmitting the signals, as well as payment mechanisms, are established. The fees were published in Vol. 75, No. 168 of the Federal Register (Part 386) (August 31, 2010).

Section 122 addresses statutory licensing for satellite retransmissions and incorporates the concept of "significantly viewed." It also sets rules for those cases where coverage is not 100 percent of any given county. Fees applicable are the same as for the retransmissions described in Section 119.

K. Conclusions from International Experience

In the countries under analysis, we see numerous different examples of how to implement must-carry and must-offer regulations. Besides those differences, however, we also found common factors that determine which of the regulations are going to be used—must-carry, must-offer, both, or none. Decisions relating to regulation choice are mainly related to: (i) dominance by FTA broadcasters, (ii) dominance by Pay TV operators, (iii) cultural or local, regional, or national content objectives and/or (iv) copyright protection. In all cases, these regulations seem to be applied when the must-carry or must-offer restrictions are operative. Notice that there is no sense in regulating a must-offer obligation when all FTA broadcasters offer their products to all networks.

When we consider (i) (the case in which there is dominance on the side of FTA broadcasters), must-offer regulations are imposed to undermine possible abuse of dominance from broadcasters. This seems the case in (a) India, where the "must provide" condition of signals should be seen in the context that each operator shall have the right to obtain the signals on a non-discriminatory basis; (b) Ireland, which in its Broadcasting Act subsection (11) states that "RTÉ, TG4 and the television service programme contractor shall ensure that their must offer services are at all times offered for re-transmission [...]" and (c) the United Kingdom, in which must-offer regulations were imposed to achieve universality objectives.

In the case of (ii) (where there is dominance on the side of Pay TV networks), must-carry regulations are imposed to undermine possible abuse of dominance by those operators. This is also the case of (a) India, where must-carry obligations are being discussed so as to "balance out the must-provide clause;" (b) Ireland, where signals from "RTÉ, TG4 and the free-to-air service provided under *section 70* by the television service programme contractor [...]" should be re-

transmitted; (c) Peru, where must-carry obligations and carriage fees are determined by a public entity; (d) Argentina, where non-satellite subscription television services shall include unencoded signals generated by the originating open television services, and (e) the United States, where the rules regarding competence sought to resolve the refusal of restricted TV operators to open up their signals to broadcast TV operators.

In other cases, the problem to resolve was related to (iii) (specific cultural content or local, regional, or national content). To solve this problem, regulation usually imposed must-carry obligations. This is the case of (a) Brazil, with must-carry obligations imposed for community and university channels; (b) Canada, with must-carry obligations for national content channels, such as the CBC English and French network services, local and regional stations, and educational services; (c) Chile, where cable operators have to incorporate in their programming, when technically possible, at least four local, community, or regional channels, and (d) Ireland, where they regulate that networks should re-transmit the Houses of the Oireachtas Channel and the Irish Film Channel.

For last, in (iv) we consider the case where the important issue is to protect the copyrights of content generators, so must-offer regulations are not considered to either (a) not infringe copyrights or (b) not provide a scheme of mandatory licensing. This is the case of Australia and the United States.

Table 1 below in Section VI, summarizes some of the key policy objectives included in MCMO regulation in the countries we have reviewed before.

V. ARE THERE BEST PRACTICES IN THE REGULATION OF MCMO CONDITIONS?

The recent public consultation, carried out by the IFT with respect to the scope of the Constitutional reform related to MCMO obligations, represents an unprecedented opportunity to provide technical recommendations to the new Mexican regulatory authority regarding how to best instill the broadcasting sector with much-needed competition. Based on the review we presented before, we believe that other countries' experiences may prove useful to the IFT in its drafting of MCMO regulations.

Common elements and mechanisms used by different agencies pursuing regulatory objectives in broadcasting that constitute best practices in the application and enforcement of MCMO regulation include:

a) There needs to be some intrinsic characteristics of the telecommunication and broadcasting sectors that explain why regulation is needed. For example, the number of operators tends to be small, with strong incentives to vertically integrate. Or, second, consumers tend to benefit from having other users consuming similar services and these consumption patterns tend to persist.

b) The multi-sidedness characteristic of telecommunication and broadcasting markets. Multi-sided platforms serve two or more groups of interdependent users (users, subscribers, audiences, advertisers, and content providers/producers), which means that any analysis that omits consideration of all sides will lead to biased results. Also, this is a sector in which fast technological innovations open up potential niches for competition in an environment of digital convergence.

c) A recognition that the ultimate goal of regulation in broadcasting is to allow audiences access to a sufficient variety of service options that meets their preferences within a competitive environment in terms of variety, price and quality. Therefore, they need to facilitate different generators of content and their advertisers to provide information and entertainment services to their desired audiences.

d) A collection of general regulatory principles that include: clarity, transparency, network interconnectivity, technological convergence, competition, and plurality to promote efficiency and economic welfare. Using the logic of a multi-sided market platform that characterizes this sector, the ultimate goal of regulation in broadcasting is to allow audiences access to a sufficient variety of service options that meets their preferences within a competitive environment in terms of variety, price and quality, and to facilitate different generators of content and their advertisers to provide information and entertainment services to their desired audiences.

e) A recognition that the purpose of imposing MCMO obligations comes from three possible adverse effects on viewers: The first adverse effect comes from the abuse of market power that is conferred by the TV premium content to its owner or acquirer because of its irreproducibility. So a must-offer obligation may be needed on popular FTA programming. The second comes from the idea that certain types of programming need to be available to as wide an audience as possible. Hence must-carry obligations may need to be imposed on Pay TV platforms. The third comes from the idea that it is desirable that viewers have access to local programs dealing with important issues in their own communities. Here, again, Pay TV broadcasters are required to retransmit local channels. Again, must-carry obligations may need to be imposed on Pay TV platforms.

f) Understanding that, although FTA and Pay TV operators compete for audiences, the first type of operator gets most of its revenues directly from advertisers while the latter derives its revenues from both subscribers and advertisers. On the other hand, both types of operators maintain a vertical relationship, as FTA TV operators are able to get more outlets for their programs by offering their signal through Pay TV, and Pay TV gets benefits by increasing the variety of content provided by the FTA TV broadcasters.

By contrast to much of the above, the proposed Mexican regulations began by making a distinction between those who provide cable Pay TV services and those who provide satellite Pay TV services. Although the cable Pay TV operators are requested to provide the local signal into the local area, the satellite Pay TV operator is allowed to retransmit any signal that covers 50 percent of the Mexican territory. This asymmetric regulation does not ensure that services meet the preferences for the two main groups of consumers: audiences and advertisers. In this way adverse effects related to a lack of localism arises among viewers and advertisers.

After analyzing the MCMO regulations across countries, we found the following common characteristics:

a) We found common factors that determine which of the regulations ought to be used: either must carry, must offer, both, or none. Those factors are related to: a) the dominance of a FTA broadcaster; b) the dominance of a Pay TV operator; c) cultural, local, regional or national content objectives; and/or d) copyright protections.

b) In our review we also found eight regulatory elements around which MCMO obligations can be organized: a) no-fee exceptions, b) the prevalence of interconnection fees, c) copyrights considerations, d) local-into-local requirements, e) independent content requirements, f) national/public content requirements, g) regional content requirements and, finally, h) public interest rules in content requirements.

c) It is interesting to note that most of these regulations have been dominated: first, by public interest rules in content requirements; second, by copyright considerations; third, local-into-local requirements; and fourth, national and regional content requirements.

d) From our perspective, Mexico's proposed regulation has been driven mainly by national/public content requirements, with a lack of consideration for the copyright and local-into-local requirements. It has also focused on a determination of the scope of mandated access with an asymmetric treatment of satellite vs. other pay TV operators. This is unique within the international context we've described.

We make the following recommendations:

a) The new regulations need to explicitly consider the rights of two types of consumers in this sector—the consumers and the advertisers—in keeping with the multi-sided nature of this market. Both types of consumers are relevant to the development of open and restricted broadcasting and all interested parties ought to be heard, including local and national advertisers (such as private and public entities, as well as political parties).

b) It is important to incorporate similar considerations to the concept of "localism" that other jurisdictions have incorporated (we include here the example of the United States, but there may be others). Audiences must have access not only to a greater variety of information, but also to relevant information that preserves and promotes plurality and addresses the specific needs of a community and enables it to maintain its own identity.

c) It is also important to preserve the right of advertisers to access niche audiences, enabling them to make themselves known to consumer groups whom they seek to inform. We must remember that, as has been established for decades in economic theory, advertising plays an important economic role that promotes efficiency.

d) It is vital that the need to establish clear rules for operators involved in restricted satellite TV not create distortions for other agents in this sector. The need to make sense of the term "national content" coming in the Eighth Transitory Article, Section I of the decree cannot ignore the rights of audiences (under Article 6. from the Constitution), advertisers, and other operators in the sector.

e) Also, the regulator should clarify considerations in addition to those made on the companies that provide restricted service using satellite platforms (vs. those using local infrastructure such as cable or spectrum). The inclusion of these considerations will make the industry run more smoothly and efficiently for all who participate in it, in compliance with the fundamental principles established in the first point of this recommendation. These considerations state that the existence of two groups of consumers must be recognized: the audience as well as national advertisers. And, in addition, it's important to recognize local authorities, including private, public, and/or political parties.

f) Finally, the regulator should not forget the importance of preserving copyright principles.

VI. TABLE 1

	Australia	Argentina	Brazil	Canada	Chile	India	Ireland	Mexico	Peru	United Kingdom	United States
No-fee exceptions	✗	✗	✗[i]	✓[ii]	✗	✓[iii]	✓[iv]	✗	✗	✗	✓[v]
Interconnection fee	✓[vi]	✗	✗[vii]	✗[viii]	✗	✓[ix]	✗	✗	✓[x]	✓[xi]	✓[xii]
Copyright considerations	✓[xiii]	✗	✗	✓[xiv]	✗	✓[xv]	✓[xvi]	✓[xvii]	✓[xviii]	✓[xix]	✓[xx]
Local-to-local requirements	✓[xxi]	✓[xxii]	✗	✓[xxiii]	✓[xxiv]	✗	✓[xxv]	✗	✗	✓[xxvi]	✓[xxvii]
Independent content requirements	✗	✓[xxviii]	✓[xxix]	✓[xxx]	✗	✗	✓[xxxi]	✗	✗	✓[xxxii]	✓[xxxiii]
National/Public content requirements	✓[xxxiv]	✓[xxxv]	✓[xxxvi]	✓[xxxvii]	✗	✓[xxxviii]	✓[xxxix]	✓[xl]	✓[xli]	✗	✗
Regional content requirements	✓	✓[xlii]	✗	✗	✓[xliii]	✓[xliv]	✓[xlv]	✗	✓[xlvi]	✓[xlvii]	✗
Public interest rules in content requirements	✓[xlviii]	✓[xlix]	✓[l]	✓[li]	✓[lii]	✓[liii]	✓[liv]	✗	✓[lv]	✓[lvi]	✓[lvii]

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[i] There is no basis if must-carry obligations are exempted of fees or if there are interconnection fees.

[ii] Prior a ruling of the Supreme Court of Canada, Canadian Radio-Television and Telecommunications Commission (CRTC) had determined that pay TV signals should negotiate carriage fees with broadcasters. In Reference re Broadcasting Regulatory Policy CRTC 2010-167 and Broadcasting Order CRTC 2010-168, Supreme Court ruled that "the provisions of the Broadcasting Act, considered in their entire context, may not be interpreted as authorizing CRTC to implement the proposed value for signal regime" and ruled that over-the-air TV should remain free for TV viewers. http://scc-csc.lexum.com/scc-csc/scc-csc/en/item/12767/index.do

[iii] Article 8 of Broadcasting Services Regulation of 2007, in its subsection (i) states that "every cable operator shall re-transmit channels operated by or on behalf of Parliament in the manner and name as may be specified by the Central Government by notification in the Official Gazette."
http://www.prsindia.org/uploads/media/vikas_doc/docs/1241499927~~Broadcasting_Services_Regulation_Bill_2007.pdf

[iv] Subsection (4) of Article 77 of the Broadcasting Act of 2009, states that "an appropriate network provider shall ensure the re-transmission, by or through his or her appropriate network, of each free-to-air television service provided for the time being by RTÉ, TG4 and the free-to-air service provided under *section 70* by the television

service programme contractor which that body or contractor requests the appropriate network provider to so re-transmit." Regarding carriage fees, subsections (7) states that "The appropriate network provider shall not impose a charge or allow a charge to be imposed in relation to the making available to a person of any service referred to in *subsection (3), (4), (5)* or *(6)* if he or she imposes a charge or allows a charge to be imposed on that person in relation to the making available of any other service to that person by means of the appropriate network concerned." http://www.irishstatutebook.ie/2009/en/act/pub/0018/

[v] According to Section 614 [47 U.S.C. 534], Subsection 10, regarding compensation for carriage, "a cable operator shall not accept or request monetary payment or other valuable consideration in exchange either for carriage of local commercial television stations in fulfillment of the requirements of this section or for the channel positioning rights provided to such stations under this section." http://www.law.cornell.edu/uscode/text/47/534

[vi] The Copyright Act of 1968 provides a statutory licensing scheme for re-transmission of free-to-air broadcast, as long as written notice is provided and remuneration is paid to the relevant collecting society.

[vii] There are no basis if must carry obligations are exempted of fees or if there are interconnection fees.

[viii] Idem.

[ix] Carriage fees are charged by cable operators in Indian broadcasting. http://www.afaqs.com/media/story/35716_Broadcasters-agree-to-reasonable-carriage-fees

[x] EGEDA is in charge of determining retransmission fees. http://www.egeda.com.pe/EPe_EGEDAPeru7.asp

[xi] In Schedule 9 of the Broadcasting Act of 1996 there is an amendment of Copyrights, Designs and Patents Act of 1988 relating to Cable Programme Services. In Section 73A it is stated that "An application to settle the royalty or other sum payable in pursuance of subsection (4) of Section 73 (reception and re-transmission of broadcast in cable programme service) may be made to the Copyright Tribunal by the copyright owner of the person making the broadcast." http://www.legislation.gov.uk/ukpga/1996/55

[xii] According to Section 614 [47 U.S.C. 534], Subsection 10, regarding compensation for carriage, "(b) a cable operator may accept payments from stations which would be considered distant signals under section 111 of Title 17 as indemnification for any increased copyright liability resulting from carriage of such signal, and (c) a cable operator may continue to accept monetary payment or other valuable consideration in exchange for carriage or channel positioning of the signal of any local commercial television station carried in fulfillment of the requirements of this section, through, but not beyond, the date of expiration of an agreement thereon between a cable operator and a local commercial television station entered into prior June 26, 1990."

[xiii] The Copyright Act of 1968 states that the maker of a television broadcast is the owner of any copyright subsisting in the broadcast (Division 5, Subdivision A, 99).

[xiv] Section 31 of the Copyright Act considers re-transmission issues. It states that "It is not an infringement of copyright for a retransmitter to communicate to the public by telecommunication any literary, dramatic, musical or artistic work," only if certain conditions are accomplished, such as transmitting without alteration, etc. http://laws-lois.justice.gc.ca/eng/acts/C-42/page-32.html#h-43

[xv] In Section 31D of the Amendment of the Indian Copyright Act of 2012 states that "Any broadcasting organization desirous of communicating to the public by way of a broadcast of by way of performance of a literary or musical work and sound recording which has already been published may do so subject to the provisions of this section." http://164.100.24.219/BillsTexts/RSBillTexts/PassedRajyaSabha/copy-E.pdf

[xvi] Article 183 of the Broadcasting Act of 2009 makes amendments to the Copyrights and Related Rights Act of 2000. Such Article describes the "digital terrestrial retransmission" as a reception and immediate retransmission on an encrypted basis without alteration by means of a multiplex of a broadcast or a cable program initially transmitted from another Member State of the EEA. http://www.irishstatutebook.ie/2009/en/act/pub/0018/

[xvii] Article 11 of Law of Radio and Television states that Secretary of Public Education would have to intervene in radio or television to protect copyrights. http://www.diputados.gob.mx/LeyesBiblio/pdf/114.pdf

[xviii] The agency in charge of setting retransmission tariffs (EGEDA) is also in charge of setting compensations for copyrights infringements. http://www.egeda.com.pe/EPe_EGEDAPeru1.asp

[xix] In Schedule 9 of the Broadcasting Act of 1996 there is an amendment of Copyrights, Designs and Patents Act of 1988 relating to Cable Programme Services. In Section 73, regarding reception and re-transmission of broadcast in cable program service, it is stated that: "The copyright in the broadcast it is not infringed (a) if the inclusion in the pursuance of a relevant requirement, or (b) if and to the extent that the broadcast is made for reception in the area in

which the cable programme service is provided and forms part of a qualifying service." http://www.legislation.gov.uk/ukpga/1996/55

[xx] An entire section of the Copyrights Law and Related Laws contained in Title 17 of the United States Code is dedicated to copyright. There are some limits to exclusive rights in secondary transmissions of broadcast programming by cable. http://www.copyright.gov/title17/circ92.pdf

[xxi] Statutory requirements introduced in 2008 require that specified regional commercial television broadcasting licensees in Queensland, New South Wales, Victoria and Tasmania broadcast at least minimum amounts of material of local significance.

[xxii] Article 65 of the Law 26.522 of Audiovisual Media Services states that open television broadcasting services shall broadcast at least thirty per cent of own production, including local news programs. http://www.afsca.gob.ar/web/Varios/ley/AUDIOVISUAL-%20MEDIA-SERVICES.pdf

[xxiii] Regulation 2006-158 enacted by the CRTC in 2006 established local programming requirements of one third for competitive market FM stations as well as a case by case system for AM stations. Programming must include local news, weather and sports material "that originates with the station or is produced separately and exclusively for the station," while excluding, for example, "programming received from another station and rebroadcast simultaneously or at a later time"

[xxiv] Law 20,422, enacted in 2010, creates broadcasting community services with the intention of allowing each community to have high quality, local, social and community broadcasts. These licenses could be issued only to non-profit organizations, municipality foundations, universities with the intention of promoting the general interest. http://www.leychile.cl/Navegar?idNorma=1013004&idParte=0

[xxv] Article 77, subsection 8 of the Broadcasting Act of 2009, states that "the Authority may require an appropriate network provider to transmit as a broadcasting service, by means of specified appropriate network maintained by the appropriate network provider, the whole or part of the programme material supplied under one or more specified community content provision contracts the holders of which are members of the local community or community of interest that is served by the said appropriate network and who request the first-mentioned appropriate network provider to so transmit the whole or, as the case may be, part that programme material." http://www.irishstatutebook.ie/2009/en/act/pub/0018/

[xxvi] Local radio stations are required to broadcast at least seven hours of local content as well as broadcasting local news, regularly refreshed and updated, at least hourly during weekday daytimes. http://consumers.ofcom.org.uk/2010/04/ofcom-deregulates-commercial-local-radio/

[xxvii] FCC requires all broadcast stations to provide news, public affairs and other programming that specifically addresses important issues facing the community.

[xxviii] In Article 65 of the Law 26.522 of Audiovisual Media Services there is an obligation for broadcasters owned by Provincial Governments, Buenos Aires City Government, municipalities and national universities that they shall broadcast educational, cultural or public interest programs equivalent to at least twenty per cent of total program contents. This obligation is not enforce to private and non-state broadcasters. http://www.afsca.gob.ar/web/Varios/ley/AUDIOVISUAL-%20MEDIA-SERVICES.pdf

[xxix] As part of a regulation in 1998, community radio broadcasting was regulated (community radio broadcasting was defined as low power and limited reach broadcasting stations directed by foundations and non-profit community associations. Additionally in the new law enacted in 2011, Law 12,485/11 it was established a minimum of 210 minutes of local content at primetime, half of which these minutes being produced by an independent Brazilian producer.

[xxx] Section 3 (1)(i)(v) of the Broadcasting Act of 1991 requires that broadcasting system as a whole to "include a significant contribution from the Canadian independent production sector." An independent production is defined as on in which a broadcasting licensee owns or controls, directly or indirectly, less than 30 percent of the equity.

[xxxi] Article 25, subsection 2 of the Broadcasting Act of 2009, states that "the authority [...] shall stimulate the provision of high quality, diverse and innovative programming by commercial, community and public service broadcasters and independent producers. http://www.irishstatutebook.ie/2009/en/act/pub/0018/

[xxxii] Section 277 of the Communications Act of 2003 requires all public service channels (that is, the six BBC channels plus the three commercial free to air national channels) to reserve at least 25% of their broadcast time to "a range and diversity of independent productions" http://www.legislation.gov.uk/ukpga/2003/21/contents

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[xxxiii] Beginning in 1975, FCC may allow a combination between a newspaper and a TV station if at least eight independently owned major media voices (major newspaper and/or full power TV stations) would remain in the market following the transaction.

[xxxiv] Australian content is regulated by mandatory standards, the Australian Content Standard 2005 (ACS). The ACS requires all commercial free-to-air television licensees to broadcast an annual minimum transmission quota of 55 per cent Australian programming between 6 am and midnight. In addition there are specific minimum annual sub-quotas for Australian (adult) drama, documentary and children´s programs.

[xxxv] Article 65 of Law 26.522 of Audiovisual Media Services states that audio broadcasters shall broadcast at least 70% of national production, while open television broadcaster shall broadcast at least 60% of national production. http://www.afsca.gob.ar/web/Varios/ley/AUDIOVISUAL-%20MEDIA-SERVICES.pdf

[xxxvi] Regarding the pay TV sector, Law 12,485/11 establishes a minimum of local content quota in order to promote national and regional culture, artistic and journalistic production, as well as stimulate independent production. This law allows the transmission of foreign programs, however, it impose a minimum of 210 minutes of local content at primetime. Additionally there is an obligation in Article 17 of the mentioned Law to include, in any subscription plan or package, one Brazilian channel for every two foreign channels offered. http://www.planalto.gov.br/ccivil_03/_Ato2011-2014/2011/Lei/L12485.htm

[xxxvii] The CRTC (Canadian Radio-Television Telecommunications Commission) enforces strict quotas for Canadian content. Private television stations must ensure that 60% of their total programming (including 50% of peak time programming) is Canadian.

[xxxviii] Article 13 of the Broadcasting Services Regulation Bill enacted in 2007, states that the share of content produced in India shall be as prescribed by the Central Government and shall not be less tan 15% of the total content of a channel broadcast during every week. http://www.prsindia.org/uploads/media/vikas_doc/docs/1241499927~~Broadcasting_Services_Regulation_Bill_2007.pdf

[xxxix] In the Broadcasting Act of 2009, there is an entire Part of the Act dedicated to Public Service Broadcasting. It mainly determines the bodies that are going to be in charge of delivering public broadcasting. http://www.irishstatutebook.ie/2009/en/act/pub/0018/

[xl] Article 21-A of Radio and Television Law, regarding objectives of public broadcasters, they should privilege national content. http://www.diputados.gob.mx/LeyesBiblio/pdf/114.pdf

[xli] Article 11 of the Ethics Code of the National Radio and Television Society, states that broadcastings between 5:00 and 24:00 should include a quota of weekly national programming of no less than 30% of the broadcasts. http://www.mtc.gob.pe/portal/comunicacion/concesion/radiodifusion/codigo_etica/sociedad_nacional_radio_tv.pdf

[xlii] Article 65 of the Law 26.522 of Audiovisual Media Services states stationary reception subscription television services: (i) shall include unencoded broadcasts and signals generated by Radio Television Argentina Sociedad del Estado, all public broadcasters and signals of the National State, and those in which the National State has an interest. Additionally, non-satellite subscription television services shall include at least one signal of own local production that satisfies the same requirements as for open television broadcasts. http://www.afsca.gob.ar/web/Varios/ley/AUDIOVISUAL-%20MEDIA-SERVICES.pdf

[xliii] Law 20,422, enacted in 2010, creates broadcasting community services with the intention of allowing each community to have high quality, local, social and community broadcasts. These licenses could be issued only to non-profit organizations, municipality foundations, universities with the intention of promoting the general interest.

http://www.leychile.cl/Navegar?idNorma=1013004&idParte=0

[xliv] Article 8 of Broadcasting Services Regulation Bill of 2007, in its subsection (ii) states that "at least two Doordashan terrestrial channels and one regional language cannel of a State in the Prime band, in satellite mode on frequencies other than those carrying terrestrial frequencies." http://www.prsindia.org/uploads/media/vikas_doc/docs/1241499927~~Broadcasting_Services_Regulation_Bill_2007.pdf

[xlv] Article 25, subsection 2 of the Broadcasting Act of 2009, states that "the authority […] shall stimulate the provision of high quality, diverse and innovative programming by commercial, community and public service broadcasters and independent producers. http://www.irishstatutebook.ie/2009/en/act/pub/0018/

[xlvi] Article 13 of Radio and Television Law, states that the Government can hold at least one channel and one radio frequency to broadcast the different traditions and culture of certain area or region. https://www.mtc.gob.pe/portal/comunicacion/concesion/mlegal/leyes/leyrtv.pdf

[xlvii] Article 32 of the Broadcasting Act of 1996 states that "The Secretary of State may by order provide for the Commission to include in any multiplex license granted in respect of one frequency to which section 28 applies such conditions relating to the broadcasting of programmes in Gaelic for reception wholly or mainly in Scotland as may be specified in, or determined by them under, the order. http://www.legislation.gov.uk/ukpga/1996/55

[xlviii] The ACMA regulates the broadcasting of political and election matters and the content of electronic communications. Among the different regulations, access for all parties, blackout period for election advertising and keeping records of political matter broadcast at the request of another person are required.

[xlix] In Article 65 of the Law 26.522 of Audiovisual Media Services there is an obligation for broadcasters owned by Provincial Governments, Buenos Aires City Government, municipalities and national universities that they shall broadcast educational, cultural or public interest programs equivalent to at least twenty per cent of total program contents. This obligation is not enforce to private and non-state broadcasters.

[l] As part of Cable TV Law regulation in 1995, community and university television channels are obligatorily transmitted by cable TV providers. Additionally every pay TV operator has the obligation of transmit public legislative channels from municipalities, estates and from the Federation.

[li] The CRTC regulates advertising in election campaigns, assuring that voters are informed during election campaigns and making equitable on-air time during a campaign. http://www.crtc.gc.ca/eng/info_sht/b309.htm

[lii] Law 20,422, enacted in 2010, creates broadcasting community services with the intention of allowing each community to have high quality, local, social and community broadcasts. These licenses could be issued only to non-profit organizations, municipality foundations, universities with the intention of promoting the general interest. http://www.leychile.cl/Navegar?idNorma=1013004&idParte=0

[liii] Article 8 of Broadcasting Services Regulation Bill of 2007, in its subsection (ii) states that "at least two Doordashan terrestrial channels and one regional language cannel of a State in the Prime band, in satellite mode on frequencies other than those carrying terrestrial frequencies." http://www.prsindia.org/uploads/media/vikas_doc/docs/1241499927~~Broadcasting_Services_Regulation_Bill_2007.pdf

[liv] In Article 77, subsection 3 of the Broadcasting Act of 2009, it is stated that "when the network is a digital system, the appropriate network provider shall ensure the re-transmission, by or through his or her appropriate network, of the Houses of the Oireachtas Channel and the Irish Film Channel." http://www.irishstatutebook.ie/2009/en/act/pub/0018/

[lv] Article 3 of the Radio and Television Law, states that the role of the State is to promote the development of broadcasting services, especially in country areas, prioritizing educational broadcasts. https://www.mtc.gob.pe/portal/comunicacion/concesion/mlegal/leyes/leyrtv.pdf

[lvi] There is a list of events, which according to Article 97 of the Broadcasting Act of 1996, are of national interest. In subsection 1 it is stated that "a listed event is a sporting or other event of national interest which is for the time being included in a list drawn up by the Secretary of State for the purposes of this Part." http://www.legislation.gov.uk/ukpga/1996/55

[lvii] Pursuant to Section 611 of the Communications Act, local franchising authorities may require cable operators to set aside channels for public, educational, or governmental use. PEG channels are not mandated by Federal Law, rather they are a right given to the franchising authority, which it may choose to exercise. http://www.publicaccess.org/cableact.html

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Lessons from the First Year of Competition Law in Ecuador

Luis Marín-Tobar[1]

I. INTRODUCTION

Ecuador's commercial and legal culture is undergoing a process of self-reflection, analysis, and evolution following the enactment of the Organic Law on Market Power Regulation and Control in October of 2011. The Law provides the first domestic framework on competition in Ecuador and was preceded by the application of Andean Community general norms on competition.[2] Pedro Paez's designation as first Superintendent for Market Power Control in September of 2012 signaled the beginning of the official practice. This paper seeks to provide an account of the exercise of powers granted to the Superintendency in the first year, as viewed from the standpoint of private legal practice, as well as to note some major areas of confusion that have been detected. The publication of this article comes shortly after the Authorities' first decision and completed investigation which resulted, on February 7, 2014, in a fine imposed on América Móvil's Ecuadorean subsidiary, telecoms operator Conecel/Claro, of $138M for abuse of dominance.

The author had the opportunity of participating in formulating observations regarding the Law and its regulations in sessions of the National Assembly—the Ecuadorian legislative branch—in panels and round table discussions organized by various business chambers and other public and private entities in Ecuador. A generalized concern was felt at that time with regard to certain recurrent issues, some of them modified in the final text approved by the Assembly, and others that remained after approval—although the fears have been unjustified in some cases.

By way of illustration, the Authority's explicit power to review personal agendas during inspections was deleted from the original text of the draft Law. The final text nevertheless allowed, with prior judicial order (to be dispatched within 24 hours), the power to review physical and virtual correspondence, including bank accounts and "other information of a confidential, privileged or secret character." This exception produced a debate regarding the Authority's power—with or without judicial authorization—to review these same types of personal agendas or documentation when prepared by the operators' internal or external lawyers, which might be subject to attorney-client privilege rules. Until resolved, this issue will give rise to discussions during inspections and, subsequently, further discussion about the evidentiary value

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[2] Decisions Nos. 608 and 616 of the Andean Community had been applied in Ecuador from 2009 to 2011 through the Office of the Under Secretary for Competition from the Ministry of Industry and Productivity.

of those documents—similar to those we have observed in European courts where the boundaries of such actions have been clarified and have evolved.[3]

To take a second example, Ecuadorian law implemented a number of prohibitions conditioned on a rule of reason analysis. In a culture where no competition regulation has previously existed, there is fear and confusion regarding the meaning and general applicability of these prohibitions, particularly those relating to vertical restraints such as exclusivity and non-compete provisions. In practice, applying a rule of reason has justified the implementation of vertical restraints in several cases, while restricting other practices. However, the private sector has sometimes generalized blanket approval from these conclusions, but then embraced certain restrictions as absolute prohibitions. This confusion has not been aided by analysis that has apparently justified the actions, but without a reasoned study of the merits.

In addition to these confusions, in the field of merger control there is an apparent discrepancy between the actual volume of transactions and stated statistics that may indicate a substantial number of cases might have not been notified to the Authority. This may be the result of (i) inadequate counseling, (ii) consent to a latent risk in favor of commercial expediency, or (iii) continued liberality from the time before concentration controls existed in Ecuador.

To take part in the beginning of a new era of law in Ecuador is a privilege and a responsibility. In the case of the public powers, this responsibility involves the Authority's fundamental task of educating business operators, general citizens, and other users regarding the new technical/economic complexities in order to enhance their own legal and commercial cultures compliance with the new regulations. From the private standpoint, the new law gives operators—large and small—the opportunity to improve their competitiveness by abiding by the rules; and gives practicing lawyers the responsibility of enhancing their knowledge to responsibly deliver their advice in such a sensitive area of law. All of the parties involved must recognize that all policies, decisions, and determinations issued by a country's competition authority can modify market structures—potentially generating greater efficiency or, if wrongly decided, distorting the market.

II. GENERAL EVALUATION OF THE FIRST YEAR

It has been a busy year for Superintendent Pedro Paez, as he needed to both set his agenda and structure his agency. Having been designated eleven months after the Law was enacted, he began his operations (i) without a budget, (ii) with no infrastructure, (iii) with deadlines and terms expiring, (iii) in improvised premises, and (iv) with the immense task of implementing an Authority of the size and importance of the Superintendency of Market Power Control. This has been no easy task. Yet, one year later, we are looking at an Authority installed in premises more in keeping with its requirements. Plus there is in place an organic structure divided into four deputy superintendencies in the first level that cover the various competitions set forth in the law, a committee for resolutions in the first instance, a general deputy department, and four general coordination offices.

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[3] Joint Cases T-125/03R and T-253/03R *Akzo Nobel Chemicals and Akcros Chemicals v Commission* [2010] Joint Cases T-289/11; T-521/11, *Deutsche Bank v Commission* [2013].

Mr. Paez and his agency employees have hosted more than twenty international seminars, built a webpage and a twitter account, and issued numerous technical rules and recommendations. Rules that regulate the labeling of transgenic food, promotional practices of the airlines, and invoicing specifications for mobile telephone services should be highlighted. The web portal has summaries of 77 cases and sectors investigated by the four deputy superintendencies, 51 of which are being processed and 26 which have been completed.

As noted above, the first decision to impose a fine just occurred. The Authority fined Conecel/Claro for abuse of market power relating to its exclusivity arrangements with landowners where telecoms masts are situated. The authority found that this agreement was an abuse of the company's market power and effectively excluded other operators from the market. The authority's fining guidelines allow it to fix fines based on total annual revenues from the year preceding the imposition of the fine, which in this case amounted to 10 percent of Conecel/Claro's total annual revenues. This is an exorbitant amount considering the reality of the local market, and will have to be paid in full even if the operator seeks administrative appeal. An appeal, according to Ecuadorean competition law, does not suspend the effects of the original decision, including payment of the fine.

In the merger control area, the website has published seven informative filings and two mandatory notices. Of particular note, in a "Concentrations Monitoring" section there is an illustrative exercise covering an analysis of a joint operation between Petroamazonas and Petroecuador, the Ecuadorean state oil companies.[4] Although not considered a concentration since there was no change of control but, rather, an intra-group restructuring, this market analysis could still be useful for people analyzing future hydrocarbon exploitation operations, particularly those deriving from changes of actual control over existing reservoirs.

Similarly, and of like importance, are the *Technical Guidelines for Analysis of Economic Concentration Operations* issued by the Deputy Superintendency of Merger control which presents important guidelines to be taken into account in concentrations control practice.

We are especially pleased to observe the joint cooperation between the Ecuadorian Intellectual Property Institute ("IEPI") and the Superintendency for Market Power Control in intellectual property and competition fora. Certainly, these are two areas with overlapping boundaries, especially regarding the development of new knowledge. Cooperation between both authorities will be particularly important during investigations involving unlawful competition and unfair practices—a power previously undertaken by IEPI, now entrusted to the Superintendency—where important intellectual property portfolios are involved.

It is also worth noting that we have observed the employment of new Superintendency employees during this time. It appears that the Authority has attracted skilled personnel with appealing remunerations, yet training and retaining those officers will be fundamental for the continuity, coherency, and congruency of ideas in the Authority's decisions.

[4] *Available at* http://www.scpm.gob.ec/wp-content/upload/2013/08/INFORME-FINAL-9-de-agosto-de-2013-PARA-WEB.pdf Access on line 16/10/2013. Emphasis added.

III. MISTAKEN CONCEPTIONS: EXCLUSIVITY

To demonstrate the need for careful training and consistency, it may be worthwhile to look indepth at one example. Exclusivity is the example into which we will delve deeper due to its importance in the Ecuadorian market.

The European Commission's guidelines relating to vertical restrictions, and particularly the introductory section, state: "The Commission aims to help companies conduct their own assessment of vertical agreements under EU competition rules. However, the **standards set forth in these Guidelines cannot be applied mechanically**, but must be applied with **due consideration for the specific circumstances of each case**. Each case must be evaluated in the light of its own facts.[5]"

This statement provides a clear conclusion, essential for everyone involved in this practice—both in the public and the private sector—to understand: There is a limit regarding general guidelines that can apply to analysis, and it is essential for operators to assess each conduct separately in order to determine if it is compatible with the legislation.

Exclusivity, perhaps, may have been the most critical issue during the first year of the new law's implementation in Ecuador. In Ecuador, historically, exclusivities have been established as common practice for provision, supply, and distribution of commodities and services. Hence, in view of the new legislation, it has become necessary to evaluate their compatibility with the new law or their possible justification.

However, although we do not know of any current investigation based on claims involving contract clauses on exclusivity, we have seen that exclusivity has been demonized as a prohibited practice *per se,* and we have even observed criteria ranking exclusivity clauses into a rigid category with dangerous general conclusions. These conclusions make no analysis of the specifics of each case—including possible efficiencies as well as specific justifications with respect to different markets.

Understanding these exclusivity agreements requires a technical analysis to balance the contractual barriers to entry that exclusivity may create vis-à-vis the benefits and efficiencies that it could bring about. In more competitive and less concentrated markets—such as the European and North American markets—there are guidelines and policies providing clear rules and exceptions on prohibitions regarding vertical restrictions when the operator's market quotas do not exceed certain specific thresholds.

In the Law, the exclusivity prohibition is discussed in articles dealing with market power abuse (Article 9(11), (19)) as well as in an article describing prohibited agreements and practices (Article 11(19)). These articles state that dominant operators, as well as other operators, might be prohibited from applying exclusivity clauses or conditions. In both cases, however, it is provided that prohibition can be voiced if the practice is justified. This means that it is not possible to automatically conclude that an operator is banned from establishing exclusivity, for instance, on sales or distributions, but only if the applicable conditions do not justify that measure. Such

[5] Communication of the Commission regarding guidelines relating to vertical restrictions. European Commission (2010C 130/01),¶3 (2010).

justification does not depend upon a subjective assessment of the operator but, rather, it requires an objective, technical, and economic study to determine that implementing the exclusivity would result in market distortion or would restrict the access of other competitors into the market or, even if that were the case, the anticompetitive effect would not be reduced by pro-competitive effects and/or other efficiencies.

It is true that competition among several operators creates advantages for the market, resulting in better prices and added value for consumers. In some sectors and conditions, nonetheless, exclusivity may be more efficient or may not affect competition. We can highlight some of the benefits granted by exclusivity:

1. Although it reduces "intra-brand" competition (between identical goods), it may encourage greater "inter-brand" competition (between competitor goods), which in the long run is more advantageous for the final consumer;
2. It can prevent free rides for "intra-brand" competitors;
3. It can create an incentive to compete in added-value services such as post-sale services; and
4. It can allow the manufacturer to maintain quality uniformity, creating a more attractive product for the final consumer.

All of the foregoing elements may justify greater efficiency if their effects are examined. Hypothetical cases make this quite clear: For example, if exclusivity is not permitted the distributor could forfeit the incentive of investing in more attractive premises, hiring more skilled personnel, or granting post-sale services because the consumer might utilize those investments in order to subsequently purchase the same product from a competitor who did not incur such costs.

A recent European case, however, highlights how these benefits must be analyzed carefully to avoid damaging the market. This case concerned a manufacturer leasing or delivering facilities free of charge in order to display and sell its products. Specifically, the European Commission studied the case of vertical restraint imposed on supermarket owners in Ireland where a dominant operator provided refrigerators for ice cream marketing. This case is noteworthy in that the Commission's analysis and conclusions made it quite clear that several elements can lead them to consider exclusivity as an exclusionary practice.

The purpose or intention of the exclusion was studied at length. In this case, exclusivity began being implemented in contracts with the entry of a new competitor into ice cream market sales where the dominant operator held more than 70 percent of that market. A study was conducted which determined that it was not practical or realistic for the owners of the stores selling the ice cream to obtain additional refrigerators for the goods of other competitors that were unable to deliver refrigerators free of charge to those stores. This study led the EC to determine that the practical effect of the exclusivity measure was to restrict access into the market to the new competitor and other competitors. The Commission's decision in year 1998 was

confirmed by the General Court and the Court of Justice of the European Community in 2006.[6] This decision provides an example of the various elements that, altogether, can create a scenario of restrictions to competition due to the implementation of exclusivity.

The foregoing example is a valuable illustration given common marketing practices, in Ecuador, for consumer goods, medicines, accessories, among others. As already mentioned, exclusivity can be an extremely useful tool in commercial practices due to a number of factors that can enhance market efficiency. Further, certain beneficial effects might exceed the anticompetitive effects created by this conduct. However, operators must evaluate these effects carefully in order to prevent adversely affecting the market, and eventually being subject to *ex officio* investigation by the Authority or to an accusation from the competitors.

IV. NON-COMPETE AGREEMENTS: A NECESSARY EVIL

Non-compete provisions are included in the same prohibition as exclusivity. It is restricted upon dominant operators and also depicted as a prohibited agreement and practice. There are, however, cases when these types of clauses are clearly justified. As with exclusivity, non-compete provisions have also been a source of debate and errors because non-compete provisions have been held as absolute prohibitions while, in some cases, they may be essential, and because certain transactions or relations beneficial for the market might provide economic justification.

As an example, in certain agency, distribution, and franchise agreements and transactions involving the transfer of knowledge or technology, non-compete agreements may be justified for a period during and even after the contract has terminated or the transaction has been performed. Without non-compete agreements, incentives to make acquisitions could disappear or be significantly deterred by the risk that, upon completion, the seller could immediately begin a competitive business, thereby reducing the value of the company sold to only its material assets.

A. Non-Compete Agreements Within the Context of Franchises and Distribution

The extent of this paper does not allow delving deeply into the special features that justify non-compete clauses in franchises and distribution contracts, but it is important to consider that such justification depends on a reasonable balance between the assets protected by the restriction and the time provided for such protection.

In the case of franchises and distribution contracts, knowledge, know-how, and/or technologies are transferred during the contractual relationship. If these are not protected, it would dissuade operators from entering into such contracts fearing that, once the technique or the technology has been learned or the information has been acquired, the franchisees or distributors might commence a competitive business taking advantage of the know-how or technology developed by the grantor.

[6] Information about the First Decision: http://europa.eu/rapid/press-release_IP-98-242_en.htm. Ruling from the Court of Justice of the European Community: http://curia.europa.eu/juris/showPdf.jsf:sessionid=9ea7d0f130d582f434ed24e5aaf786b8ab67ff261.e34KaxiLe3eQ40LaxqMbN4Oahy/Te0?text=&docid=65800&pageIndex=0&doclang=ES&mode=lst&dir=&occ=first&part=1&cid=291255.

Terms regarding restrictions can vary substantially. To a great extent, the lawfulness of restrictions both during the contract term and after contract termination will depend on the type of franchise and of the goods or services involved. In Ecuador, these types of contracts are atypical or unnamed, and no specific regulation regarding them exists. Thus, it is common to find mere distributor relationships designated as franchises, in which case a justification of a non-compete type of restriction might be even more limited.

Legislation from other countries provides guidelines regarding the length of periods that may be considered justified when implementing non-competing clauses, depending on the value of the assets being transferred. Such rules should be implemented—without them, the impossibility of protecting the goodwill and the know-how transferred during this type of contractual relations discourages the use of those contracts.

B. Non-compete Within the Context of Concentrations

Doctrine and international case law have developed clear guidelines in the area of non-compete clauses within concentrations. It is useful to refer to the communication issued by the European Commission in July of 2001[7] establishing restrictions directly relating to concentration operations that are deemed to be necessary. This document provides lessons from the experience acquired by the European Commission after several decades of analyzing hundreds of thousands of concentrations for which they found permissible restrictions and issued guidelines for operators to create further legal security regarding their operations.

In essence, the document seeks to protect the transferred value with reasonable measures that do not have less harmful or restrictive alternatives on competition. If such intangible elements cannot be protected, the value of the transaction would not exceed the value of the material assets. In other words: To be justified, restrictions ought to have direct, necessary, and objectives relative to the operation.

Further, when a transfer deriving from the transaction includes know-how or technologies that subsequently may be reproduced, a two-year restriction or even greater periods are justified depending on the type of know-how and/or the value of the commercial secrets transferred. Restrictions are allowed regarding the seller opening a competitor company and restrictions are even allowed on buying shares in competitor companies if such shares grant managerial functions or a material influence on the competitor company.

The technical guidelines issued by the Deputy Superintendency for Concentration Control from the Superintendency for Market Power Control make no reference to this issue, and the majority of authorized transactions have not resulted in developing guidelines. Therefore, regarding this issue, it will be necessary to follow up with new decisions, regulations, or directions to be issued by the Authority.

[7] Communication from the Commission on directly related and necessary restrictions for concentration operations (2001/C188/03): *Available at* http://eur-lex .europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2001:188:0005:0011:EN:PDF.

V. NOTIFIED CONCENTRATIONS VERSUS PERFORMED CONCENTRATIONS

As a curious piece of information, the first transitory provision of the Regulations to the Law ordered mandatory notice of all concentration operations carried out for the period from October 11, 2011 until the Superintendent took office on September 6, 2012, with no exception, including those that did not require notice on the basis of the thresholds of the Law. This provision sought to overcome the practical impossibility of filing transactions during that period, despite there being a legal obligation to do so. Aimed at covering all concentrations, the provision even included those that did not require notice because they did not surpass the thresholds established in the Law. In a strictly legal sense, in practice this would have led to the obligation of giving notice of all kinds of concentrations, including a purchase of a convenience store by a tiny operator, or the common administration of companies with no substantial turnover from the standpoint of the concentration thresholds.

However, we noticed that the volume of concentration notices published by the Authority in its web portal or in its report of first-year activities seemed not to be in keeping with the actual concentrations subject to mandatory notice that must have truly taken place since the Law came into effect, especially taking into consideration another transitory provision of the Law that obligated financial sector entities to alienate their non-financial assets by July 13, 2012 and the evident change of control that should have existed and made filing and approval mandatory.

VI. CONCLUSIONS AND REFLECTIONS

Competition law is not an absolute science. Business practices deserve responsible and careful in-depth study by the operators from both a legal and economic standpoint to evaluate their legality. Serious economic liability may arise from the substantial fines imposed if a conduct is mistakenly considered to be permissible, or from opportunity costs that could result from a conduct mistakenly considered to be prohibited when it may have been justified by providing a competitive solution for the operator and that, if correctly evaluated, would have permitted the operator to compete with greater efficiency in the market.

Ecuador's first year of practice reflects precisely these issues, confusion and mistakes, and this reflective analysis determines the need to further promote and study the field in our culture.