July 28, 2014

United States Sentencing Commission
One Columbus Circle, NE,
Suite 2-500, South Lobby
Washington, D.C. 20002-8002

Attention Public Affairs - Priorities Comment

Dear U.S. Sentencing Commission:

We are writing pursuant to the Commission's Federal Register Notice of Proposed Priorities and Request for Public Comment, June 2, 2014, in which the Commission is seeking public comment on proposed priority policy issues for the amendment cycle ending May 1, 2015.[1] The Commission identified as being among it's tentative priorities: "2) Continuation of its work on economic crimes, including... (C) a study of antitrust offenses, including examination of the fine provisions in §2R1.1 (Bid-Rigging, Price-Fixing or Market Allocation Agreements Among Competitors); and (D) consideration of any amendments to such guidelines that may be appropriate in light of the information obtained from such studies."

The American Antitrust Institute (AAI) is an independent non-profit education, research, and advocacy organization. Our mission is to increase the role of competition, assure that competition works in the interests of consumers, and challenge abuses of concentrated economic power in the American and world economy. We promote the vigorous use of antitrust as a vital component of national and international competition policy.[2]

We are pleased the Commission is considering a study of the Guidelines' antitrust fine provisions. In this comment we urge the Commission to reconsider a crucial empirical finding it made in 1987 that has become a lynchpin of the formula used to calculate fines for collusion offenses. The 2013 Guidelines Manual, Chapter Two - Offense Conduct, Part R - Antitrust Offenses, Section 2R1.1, Commentary 3, reads as follows:

> "3....In selecting a fine for an organization within the guideline fine range, the court should consider both the gain to the organization from the offense and the loss caused by the organization. It is

[1] *Federal Register Notice of Proposed Priorities and Request for Public Comment*, 79 FR 31409 UNITED STATES SENTENCING COMMISSION 1 (Jun. 2, 2014), http:/ http://www.ussc.gov/sites/default/files/pdf/amendment-process/federal-register-notices/20140602_FR_Proposed_Priorities.pdf. The American Antitrust Institute previously submitted comments to the U.S. Sentencing Commission on this topic, on July 8, 2013. *See American Antitrust Institute Calls on US Sentencing Commission to Double Cartel Fines*, AMERICAN ANTITRUST INSTITUTE (Jul. 8, 2013), http://www.antitrustinstitute.org/sites/default/files/USSCAAILetter.pdf.

[2] Founded in 1998, AAI is a 501(c)(3) tax exempt Washington, D.C. corporation. For more information, *see* http://antitrustinstitute.org.

2919 ELLICOTT ST, NW • WASHINGTON, DC 20008
PHONE: 202-276-6002 • FAX: 202-966-8711 • bfoer@antitrustinstitute.org
www.antitrustinstitute.org

> estimated that the average gain from price-fixing is 10 percent of the selling price.... The purpose for specifying a percent of the volume of commerce is to avoid the time and expense that would be required for the court to determine the actual gain or loss.... "[3]

The antitrust enforcers almost always use this 10% estimate when they negotiate cartel fines with defendants. It effectively has become a strong presumption that in practice Defendants rarely challenge and the Courts routinely accept.[4]

Our comment makes three important points about the U.S. Sentencing Guidelines' (USSGs') cartel overcharge presumption. First, the evidence demonstrates there currently is significant underdeterrence of price fixing and other anticompetitive forms of horizontal collusion. Second, the general approach to calculating cartel fines embodied in the USSGs, which utilize a specific presumed overcharge, is sound and in the public interest. Third, the 10% cartel overcharge presumption in the Guidelines is much too low to achieve deterrence. The best evidence demonstrates that the Commission should double it to 20%. This change would move the Guidelines in the direction of both recent and historical evidence on average overcharges likely to result from collusion, yet still be a conservative resolution of the issues. Raising the 10% presumption should improve the overall level of cartel deterrence and raise consumer welfare.

The Current Level Of Cartel Sanctions Is Suboptimal

The United States imposes a diverse arsenal of sanctions against cartels.[5] Nevertheless, cartels probably are caught and convicted no more than 25% of the time.[6] Moreover, as the third section of this comment will show, illegal collusion historically has usually resulted in large overcharges.[7]

To analyze whether the current level of sanctions is optimal, Connor & Lande use the standard optimal deterrence approach.[8] This assumes corporations and individuals contemplating illegal

[3] *See* United States Sentencing Commission, Guidelines Manual, §2R1.1 (Nov. 2013), http://www.ussc.gov/sites/default/files/pdf/guidelines-manual/2013/manual-pdf/2013_Guidelines_Manual_Full.pdf. Commentary 3 also explains why this 10 percent figure is doubled to account for a number of factors before it is included in the fine determination calculations. "The loss from price-fixing exceeds the gain because, among other things, injury is inflicted upon consumers who are unable or for other reasons do not buy the product at the higher prices. Because the loss from price-fixing exceeds the gain, subsection (d)(1) provides that 20 percent of the volume of affected commerce is to be used in lieu of the pecuniary loss under §8C2.4(a)(3)." We believe this doubling is warranted due to a number of factors, including the allocative inefficiency effects of market power, the umbrella effects of market power, and the fact that neither inflation nor prejudgment interest is explicitly considered in fine calculations even though many years typically pass between cartel overcharges and the imposition of the fine. *See* John M. Connor & Robert H. Lande, *Cartels as Rational Business Strategy: Crime Pays*, 34 CARDOZO L. REV. 427, 455-62 (2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1917657.

[4] *See* John M. Connor & Robert H. Lande, *How High Do Cartels Raise Prices? Implications for Optimal Cartel Fines*, 80 TULANE L. REV. 513, 524 (2005), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1917657.

[5] These include criminal fines and restitution payments for the firms involved, and prison, house arrest and fines for the corporate officials involved. Both direct and indirect victims can sue for mandatory treble damages and attorney's fees. For analysis of these issues, *see id*.

[6] *See* Connor & Lande, *supra* note 3, at 462-68. Their review of the literature shows a probability of 20-24%.

[7] *Id*. at 427.

[8] *Id*. at 431-47. This study also employed a behavioral approach that reached the same conclusions. *Id*.

collusion will be deterred only if expected rewards are less than expected costs, adjusted by the probability the illegal activity will be detected and sanctioned. To undertake this analysis they first calculate the expected rewards from cartelization using a new and unique database containing information on 75 cartel cases. They survey the literature to ascertain the probability cartels are detected and the probability detected cartels are sanctioned. They calculate the size of the sanctions involved for each case.[9]

Their analysis shows that, overall, United States' cartel sanctions are probably only 9% to 21% as large as they should be to protect potential victims of cartelization optimally.[10] This means that, despite the existing sanctions, collusion remains a rational business strategy. Cartelization is a crime that on average pays. In fact, it pays very well. Significantly higher cartel sanctions should be imposed, and this should save consumers many billions of dollars each year.

The Guidelines' Use of A Specific Overcharge Presumption To Calculate Fines Has Been Wise

The USSGs for antitrust have, since their inception, employed a presumption as to the size of cartel overcharges, and for more than twenty years have used this as the lynchpin of its fine calculations. This approach has proven to be extremely desirable and has constituted an important enforcement tool. The structure of the USSGs makes fine levels more predictable for would-be cartelists. The 10% starting point, together with other specific adjustments, make expected fines relatively easy to compute in advance of a guilty plea. Such predictability assists with the general deterrence of anticompetitive collusion, and reduces enforcement and administrative costs significantly.

The present Guidelines do not simply incentivize those specific cartel members that have been caught to not do it again. The fines also deter would-be cartelists generally. The goal of general deterrence is especially important for a crime like price fixing which is extremely difficult to detect and prove.[11] The past can never truly be corrected through fines (indeed, that is what private actions are for). Thus, consumer welfare is better served by preventing future price fixing throughout our economy than to calculate the "correct" penalty for past crimes.

The alternative to Guidelines built upon average injuries in the past would be a case-by-case approach. However, this would require prosecutors to calculate the precise size of the overcharges in every case beyond a reasonable doubt and set fines to reflect these firm-specific overcharges. This approach superficially might appear to be "fair" to each defendant, but case-by-case overcharge calculations in fact have many disadvantages. Predictability for business would decrease and the deterrent effects of the Guidelines would be significantly undermined. The *actual* amounts by which cartels raised prices or are fined, years after the illegal collusion occurs, is much less important from a public policy perspective. Rather, what is crucial is the belief of potential cartelists *ex ante* as to how much they can increase profits, their likelihood of being caught, and the severity of likely punishment. To the extent there is rational forethought,

[9] These include corporate fines, individual fines, payouts in private damage actions, and the equivalent value (or disvalue) of imprisonment or house arrest for the individuals convicted. *Id*.
[10] *Id*. at 474-84.
[11] For the importance of optimal cartel deterrence, *see id. passim*. For the probability of cartel detection, *see id*. at 462-68.

these predictions guide would-be cartelists' decision as to whether they will attempt to form a cartel.

Case-by-case calculations also would be much more expensive for taxpayers (and for defendants) than the current system.[12] Moreover, although preliminary calculations are common, full and final overcharge calculations of overcharges have rarely been done in DOJ or in private damages cases. Although thousands of private damage actions have been filed in cartel cases, almost every private cartel damages suit settles or is dismissed before an overcharge can be calculated by a neutral observer and made part of the public record of the case.[13] As a practical matter, should the Antitrust Division be required to prove the size of the overcharges in each case, it would be unable to bring as many cases. This would lead to less cartel deterrence and would harm consumers and the economy generally. The only ones who would benefit would be cartelists and their attorneys and economists.[14]

Another advantage of the USSG' current presumption-based approach is that the parties can, if they wish, contest it. As the Guidelines' Commentary notes, in special cases a different overcharge amount can be used: "In cases in which the actual monopoly overcharge appears to be either substantially more or substantially less than 10%, this factor should be considered in setting the fine within the guideline fine range."[15] Indeed, the Guidelines are themselves only advisory, not binding, although their judgments cannot be lightly disregarded.[16] Because, as the next section will demonstrate, the overwhelming majority of cartel overcharges greatly exceed 10%, it is not surprising that defendants rarely challenge its use. But the possibility that defendants can contest it in appropriate cases is another reason for the USSG to retain a rebuttable overcharge presumption.

The Guidelines' Presumption That Price Fixing Raises Prices by 10% Should Be Doubled

[12] It is impossible to determine how much litigation costs would increase if overcharges were ascertained in every case, but surely it would be substantial. It is often difficult to determine whether or when a group of firms conspired to fix prices. The ease of answering this question pales, however, compared to the costs of ascertaining and proving in court how much prices rose as a result of a cartel. Under the current fining approach the Department of Justice usually only needs to prove that collusion occurred and to show the amount of commerce involved. If the government were also required to demonstrate how high prices rose as a result of the cartel, its burden would increase substantially. Although it is impossible to know whether the amount of prosecutorial resources required to successfully prosecute a cartel would, e.g., double or sextuple, it is clear that the increase would be significant. So would the amount of time required to complete the case.

[13] The case-by-case approach to calculating cartel damages - under the pressures of a litigation setting - is so difficult, risky, expensive, controversial, uncertain, and lengthy that final estimates of damages by the parties are put off as long as possible. Connor & Lande tried to find every final litigated cartel overcharge case in history but - perhaps surprisingly - were only able to find 25. *See* Connor & Lande, *supra* note 4, at 556. Of course, many private cartel cases are dismissed because they lack merit. For a discussion of settlement in this context, and why settlement amounts are likely to be an extremely unreliable guide as to the size of the underlying cases' overcharges, *see id.*

[14] The burden of proving overcharges in each case would be so large that if political issues were to require the Commission to choose between maintaining the current 10% overcharge presumption and switching to a case-by-case analysis, we would urge the Commission to maintain the current 10% presumption, as removal of a presumption in cartel cases would be more damaging than the realistic increase in penalties that would result from a case-by-case approach would be beneficial.

[15] *See* United States Sentencing Commission, Guidelines Manual, §2R1.1 (Nov. 2012), *available at* http://www.ussc.gov/sites/default/files/pdf/guidelines-manual/2012/manual-pdf/2012_Guidelines_Manual_Full.pdf.

[16] *See* Kimbrough v. United States, 552 U.S. 85, 109 (2007).

This 10% presumption has been in the Sentencing Guidelines since their inception,[17] and to our knowledge the Commission has never seriously re-examined whether 10% is the best figure to use. Although we do not know how the Commission arrived at 10%, it may be significant that when the Commission was in the process of formulating these Guidelines the then-Assistant Attorney General for Antitrust, Douglas Ginsburg, stated in a Hearing before the Sentencing Commission that "price fixing typically results in price increases, that has harmed the consumers in a range of 10 percent of the price...."[18] We know of no other estimates presented to the Commission at that time, and the Commission might well have accepted and used AAG Ginsburg's estimate. We note that Ginsberg's estimate is unlikely to have included any international cartels, the type that now accounts for most U.S. cartel fines and that usually generate the highest overcharges.

In recent years a number of empirical studies have re-examined this issue. These studies have shown that price fixing usually raises prices by significantly more than 10%.

The most comprehensive of these analyses has been the recent study by Professor John Connor.[19] This surveyed more than 700 published economic studies that contain 2,041 quantitative estimates of the overcharges by hard-core cartels. His primary findings are that the *median* long-run overcharge for all types of cartels over all time periods has been 23%, and that the *mean* overcharge has been 49%.[20] There was no significant trend in cartel markups in recent years --the median and mean figures for collusion episodes ending since 2000 was 20% and 39%.[21] The mean of the average overcharge figures, 49%, is much higher than the median figure due to the presence of a number of extremely large overcharges in the sample.[22] Perhaps the most striking result is that 79% of cartel overcharges have been above the USSG's 10% presumption, and 56% have been above 20%.[23]

The overwhelming source of overcharge estimates in Connor's study is publications by economists. Connor & Lande also used a very different source to find cartel overcharges: final verdicts in litigated United States cartel cases. Because government enforcers are not usually required to calculate the actual overcharges in their cartel cases and because almost every private antitrust suit for damages settles or is dismissed before an overcharge can be calculated by a

[17] For the history of the presumption, *see* Connor & Lande, *supra* note 3, at 524-26.
[18] *See Sentencing Options: Hearing Before the United States Sentencing Commission (July 15, 1986)*, in UNITED STATES SENTENCING COMMISSION: UNPUBLISHED PUBLIC HEARINGS 1986, at 15 (1988).
[19] *See* John M. Connor, *Cartel Overcharges*, 29 RESEARCH IN LAW & ECONOMICS 249 (2014).
[20] *Id*. These figures include the 6% of cartels that were ineffective. Because these cartels are less likely to have been challenged, the 49% figure is conservative.
[21] *Id*. at Table 5 (median results) and Table 7 (mean results).
[22] *Id*.
[23] For additional results see Appendix 1, which is based upon Table 6 in John M. Connor, *Cartel Overcharges*, *supra* note 19. Partly in response to this evidence on cartel overcharges, the European Commission in 2006 substantially revised its fining guidelines. They significantly raised their "starting point" percentage (roughly similar to the USSC's 10% overcharge presumption) and toughened many of the factors that enhance fines for hard-core price fixing. The 2006 revisions are one of the main reasons that EC cartel fines – previously lower than comparable U.S. fines -- have surpassed U.S. cartel fines in size and severity. *See generally Fines for Breaking EU Competition Law*, EUROPEAN COMMISSION (Nov. 2011), http://ec.europa.eu/competition/cartels/overview/factsheet_fines_en.pdf.

neutral fact-finder and made part of the public record of the case, [24] there have been only a very small number of litigated cartel verdicts. The authors were only able to find 25 litigated final cartel verdicts issued since 1890 to analyze. The cartels in these cases were found to have had median overcharges of 22% and average overcharges of 31 percent.[25]

Thus, the two sources (economic studies and cartel verdicts) produced very similar median cartel overcharges, of 23% and 22% overall. The average overcharge results were 49% for the economic studies and 31% for the verdicts. The Guidelines currently presume the "average" gain from collusion is 10%, and the corresponding "average" overcharges computed in the two samples we cite (economic studies and verdicts in cases) are 49% and 31%. Accordingly, our recommendation that the Commission double the 10% presumption is conservative.

Conclusions

When the Commission formulated its estimate that price fixing on average raises prices by 10% it did so on the basis of the best evidence available in 1987.[26] But the evidence that has accumulated during the 27 years since then strongly suggests this estimate is significantly low.

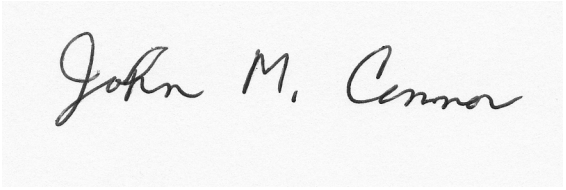
The 10% presumption is of course a crucial underpinning of antitrust fine calculations. Raising it to 20% would double the amounts in the recommended antitrust fine range. In total, corporate antitrust fines have been between $272 million and $1.472 billion each year since 2005.[27] Doubling the 10% presumption would result in a considerable increase in the funds available to the Crime Victim's fund, for compensating victims of violent crimes, as well as lead to improved deterrence of price fixing and other cartel behavior.[28]

For these reasons the American Antitrust Institute urges the U.S. Sentencing Commission to retain the general approach of employing a specific overcharge presumption when it calculates fines for price fixing, but to double the 10% overcharge presumption contained in Section 2R1.1 of the Guidelines.

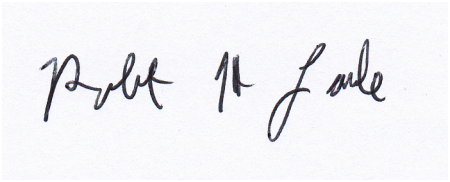
[24] *See* Connor & Lande, *supra* note 3, at 551-55. For a discussion of settlement in this context, and why settlement amounts are likely to be an extremely unreliable guide as to the size of the underlying cases' overcharges, *see id.*
[25] *Id*. at 556.
[26] There is evidence that the post World-War-II years up to the mid 1970s were years during which overcharges were at historic lows – 40% below average (*See* Connor & Lande, *supra* note 3, at 513, Table 4, row 4). Therefore, the 10% average overcharges calculated by the DOJ in the 1980s could have been accurate for the time, but the period observed was atypical.
[27] *See Antitrust Division Workload Statistics FY 2004-2013*, U.S. DEPARTMENT OF JUSTICE, *available at* http://www.justice.gov/atr/public/workload-statistics.html.
[28] For a more detailed analysis of the issue of the optimal deterrence of cartels, *see* Connor & Lande, *supra* note 3, *passim*. The authors suggest, inter alia, adjusting fine levels based upon cartel overcharges to present value to compensate for the effects of inflation.

Respectfully submitted,

Albert A. Foer
President
American Antitrust Institute



John M. Connor
Senior Fellow, American Antitrust Institute
and Professor Emeritus
Purdue University



Robert H. Lande
Director, American Antitrust Institute
and Venable Professor of Law
University of Baltimore School of Law