

ANTITRUST TRADE AND PRACTICE

Expert Analysis

## Cartel Deterrence At U.S. Sentencing Commission

In June 2014, the U.S. Sentencing Commission proposed a list of priorities for the Sentencing Guidelines amendment cycle ending May 1, 2015.<sup>1</sup> This proposal calls for a study of antitrust offenses and for examination of the penalty provisions in Section 2R1.1 of the U.S. Sentencing Guidelines (the antitrust sentencing guidelines) that relate to bid-rigging, price-fixing, and market allocation agreements among competitors.

A debate about the sufficiency of the antitrust sentencing guidelines for achieving optimal cartel deterrence has percolated among academics since at least 2005.<sup>2</sup> Scholars have weighed in on various aspects of antitrust sentencing, from the implications of the prevailing Chicago-school goal of “optimal deterrence,”<sup>3</sup> to the appropriate presumption for cartel gains,<sup>4</sup> to exhortations for paradigmatic shifts in how governments punish cartel behavior.<sup>5</sup> Unsurprisingly then, the presence of an antitrust priority in the commission’s proposal inspired several thoughtful public comments on possible reforms.



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Practitioners should be aware of three submissions, one from the American Antitrust Institute (AAI), another from the Criminal Division of the U.S. Department of Justice, and a third from Judge Douglas H. Ginsburg of the U.S. Court of Appeals for the District of Columbia Circuit and FTC Commissioner Joshua D. Wright. These submissions set forth a well-informed, if preliminary, debate on whether the existing antitrust sentencing guidelines are effective. The conversation embodied in these comments should evolve into broader questions about whether increased antitrust sanctions are truly the most effective way to deploy government resources in pursuit of improved cartel deterrence. Certainly, it is an area that practitioners should closely follow.

### Organizational Fines

The first axis of debate in response to the commission’s

proposal was whether the organizational fine recommendations in the antitrust sentencing guidelines promote effective deterrence. Organizational fines have increased over time. From 1987 to 2004, the maximum statutorily permitted organizational fine for antitrust violations rose from \$1 million to \$100 million.<sup>6</sup> Likewise, the average fine levied against antitrust offenders increased from \$480,000 from 1990 to 1994, to over \$44 million around 2009.<sup>7</sup>

Currently, the antitrust sentencing guidelines set base fine recommendations for organizational defendants at 20 percent of the volume of affected commerce.<sup>8</sup> The 20 percent figure serves as a proxy for pecuniary loss caused by the cartel, and is intended to conserve judicial resources by forgoing the need to determine actual loss.<sup>9</sup> The 20 percent figure is based in part on the commission’s presumption that the estimated average gain from horizontal conduct is 10 percent of the selling price.<sup>10</sup> The remaining 10 percent is based on the assumption that overcharge alone does not fully reflect harm “inflicted upon consumers who are unable or for other reasons do not buy the product at the higher prices.”<sup>11</sup>

Against this backdrop, on July

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28, 2014, the AAI submitted a comment to the commission criticizing the current level of cartel sanctions as “suboptimal” and calling for an increase in the 10 percent specific overcharge presumption used to formulate the 20 percent base fine figure.<sup>12</sup> The thrust of the AAI’s argument is that, although the practice of using a presumed overcharge is “sound and in the public interest,” the existing 10 percent presumed overcharge is “much too low to achieve deterrence.”<sup>13</sup> The AAI recommends that the Commission double its existing presumption for cartel overcharges from 10 to 20 percent, and increase the base fine percentage accordingly.<sup>14</sup>

In response to the AAI, the Justice Department filed a letter on July 29, 2014 indicating its belief that the current recommended organizational fines are appropriate.<sup>15</sup> To rebut the AAI’s call for an increased overcharge presumption, the Justice Department pointed to the commission’s direction that, “[i]n cases in which the actual...overcharge appears to be either substantially more or substantially less than 10 percent, this factor should be considered in setting the fine within the guideline fine range.”<sup>16</sup> This instruction, along with literature indicating that the average cartel overcharge is not as high as the AAI’s citations would indicate, led the Justice Department to conclude that it does “not believe it would be a worthwhile expenditure of resources to put any process in motion to increase the 10 percent presumption marginally.”<sup>17</sup>

The Justice Department’s reticence to support an increase in organizational fines prescribed by the antitrust sentencing guidelines demonstrates awareness of the possible downsides to over-deterrence. As Judge Ginsburg and Commissioner Wright observe,

toughening organizational cartel sanctions may deter potentially efficient conduct such as non-exclusive vertical restraints, or may unnecessarily raise compliance costs, which firms eventually pass along to consumers.<sup>18</sup> Given the Justice Department’s existing discretion and considerable hesitance, change on the organizational fine front appears unlikely.

### Sanctions for Individuals

A second suggestion in response to the commission’s proposal came in a July 28, 2014, submission from Judge Ginsburg and Commissioner Wright.<sup>19</sup> In addition to highlighting that harsh organizational fines potentially impose costs associated with over-deterrence, Ginsburg and Wright conclude that there is little evidence to show that such fines even deter cartel behavior. Given this reality, they suggest that the commission shift the target of the antitrust sentencing guidelines away from organizations and toward individuals in those organizations responsible for the illegal conduct.<sup>20</sup>

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Broader questions arise about whether increased antitrust sanctions are truly the most effective way to deploy government resources in pursuit of improved cartel deterrence.

To be sure, the antitrust sentencing guidelines already recommend strong jail penalties for culpable individuals. Antitrust offenders face a base guideline jail time of 10 to 16 months, rising to as many as 87 to 108 months if the offender is guilty of bid-rigging or the cartel activity affected a volume of commerce over \$1.5 billion.<sup>21</sup> In addition to jail time, individual offenders face stiff fines

in the minimum amount of \$20,000, possibly rising to 1 to 5 percent of the affected volume of commerce.<sup>22</sup>

Despite the existence of these strong penalties, Ginsburg and Wright suggest revising the antitrust sentencing guidelines to include higher individual fines and jail sentences and to add corporate disqualification penalties. At the heart of their proposal is a granular view of the offending firm as consisting of distinct actors, including the shareholders (who are relatively incapable of preventing antitrust violations), directors and officers (who have compliance and monitoring obligations and may be negligent in instances of antitrust violations), and the perpetrator.<sup>23</sup> They argue that the antitrust sentencing guidelines should subject the perpetrator to criminal penalties, and subject negligent, culpable, or complicit directors and officers to fines and corporate debarment.<sup>24</sup> They suggest that this more granular view of an offending firm creates better incentive structures by rewarding strong antitrust compliance.<sup>25</sup>

Yet, Ginsburg and Wright’s proposed solution of harsher individual sanctions may suffer from the same challenges that they identify with respect to harsh organizational fines. If the commission adopts Ginsburg and Wright’s proposal, future critics may well conclude, as Ginsburg and Wright do about high organizational fines, that harsh penalties against individuals deter efficient conduct and generate no empirical evidence of successful cartel deterrence. Imposing harsh antitrust penalties on individuals, particularly individuals who took no part in the conduct at issue but who are adjudged negligently culpable and debarred on such grounds, may also stoke inefficient zeal for compliance programs.

Further, shifting the burden of harsh sanctions from the organization to individuals serves as a balm for the perception of cartel underdeterrence, but does not have any quantifiable measure of success. Ginsburg and Wright themselves acknowledge that “given the inherent uncertainty about the probability of detection and other key empirical inputs, it is likely impossible to pinpoint the optimal level of total antitrust sanctions, much less to identify precisely the mix of potentially available sanctions that would lead to the uniquely efficient level of deterrence.”<sup>26</sup>

### The Broader Debate

The conversation surrounding the commission’s proposal focused narrowly on sanctions as the default form of cartel deterrence. However, interested parties can and should think about the goal of cartel deterrence more broadly. Practitioners, legislators, businesspeople, the commission, media, and other government agencies should reconsider the optimal level of sanctions and think about the proper allocation of finite government resources between sanctions and alternative programs that may achieve the same goal of cartel deterrence. The importance of this broader conversation is especially critical as the commission now weighs studying changes to the antitrust sentencing guidelines against other pressing priorities.

All interested parties may find value in discussing as an alternative to antitrust sentencing reform the deployment of government resources to educate the public about the ills of cartels. In studying media coverage of cartel enforcement from 1990 to 2009, Daniel Sokol, law professor at the University of Florida Levin College of Law, found that, “relative to other types of financial crimes, such as accounting fraud, the public seems unaware

or uninterested in cartel activity. The lack of public awareness and the resulting lack of social penalties impact deterrence and detection.”<sup>27</sup> An education and outreach program would address the low existing social costs and public awareness associated with cartel behavior, altering the cost-benefit calculus that underpins the theory of optimal cartel deterrence.

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This approach also has several incremental benefits when compared to tougher sanctions. First, it raises both the social costs of cartel behavior and likelihood of detection. Increasing sanctions does little to increase the likelihood of detection. In contrast, outreach programs raise the expected costs of cartel behavior by creating strong and ubiquitous social norms, and also increase the likelihood of detection by creating a compliance culture.<sup>28</sup> Second, unlike increased penalties, outreach would not risk raising inefficient compliance costs or deterring otherwise efficient conduct. This second consideration is especially important because cartels are unobservable and, in turn, deterrence is unmeasurable. Because the benefits of a given deterrence regime are hard to quantify, the costs of such a regime take on added importance in any analysis of the regime’s viability.

Antitrust sentencing reform certainly has its place in what should be a wide-ranging conversation about how to combat cartels. That

said, although public outreach is not a panacea, it deserves more consideration as the commission and other interested parties look at the most appropriate ways to deploy limited government resources to improve cartel deterrence.

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1. U.S. Sentencing Commission, Notice and Request for Public Comment on Proposed Priorities for Amendment Cycle, 79 Fed. Reg. 31409.

2. See John M. Connor and Robert H. Lande, “How High Do Cartels Raise Prices? Implications for Optimal Cartel Fines,” 80 Tul. L. Rev. 513, 522 (2005).

3. Daniel Sokol, “What Practitioners Think About Enforcement,” 78 Antitrust L. J. No. 1, at 201 (2012).

4. See John M. Connor and Robert H. Lande, “Cartels as Rational Business Strategy: Crime pays,” 34 Cardozo L. Rev. 427 (2012); John M. Connor, Cartel Overcharges, 29 Research in Law & Economics 249 (2014).

5. Douglas H. Ginsburg and Joshua D. Wright, Antitrust Sanctions, Competition Policy International, Vol. 6, No. 2 (Autumn 2010), available at [http://www.uscc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/Ginsburg\\_Wright.pdf](http://www.uscc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/Ginsburg_Wright.pdf).

6. Ginsburg and Wright, *supra* note 5, at 4.

7. *Id.*

8. U.S. Sentencing Guidelines Manual §2R1.1(d) (2014); see also U.S. Sentencing Guidelines Manual §8C2.4, cmt. n.5 (2014).

9. U.S. Sentencing Guidelines Manual §2R1.1 cmt. n.3 (2014).

10. *Id.*

11. *Id.*

12. American Antitrust Institute, Letter to the United States Sentencing Commission, July 28, 2014, at 3-5, available at <http://www.uscc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/AAI.pdf>.

13. *Id.* at 2.

14. *Id.* at 4-6.

15. U.S. Department of Justice, Criminal Division, Letter to the Honorable Patti B. Saris, July 29, 2014, at 24, available at <http://www.uscc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/DOJ.pdf>.

16. U.S. Sentencing Guidelines Manual §2R1.1, cmt. n.3 (2014).

17. See U.S. Department of Justice, *supra* note 15, at 24-25.

18. Ginsburg and Wright, *supra* note 5, at 8.

19. Douglas H. Ginsburg and Joshua D. Wright, Letter to United States Sentencing Commission, July 28, 2014, available at [http://www.uscc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/Ginsburg\\_Wright.pdf](http://www.uscc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/Ginsburg_Wright.pdf).

20. See *id.*

21. U.S. Sentencing Guidelines Manual §2R1.1(b)(1) (2014); see also Beryl A. Howell, Sentencing of Antitrust Offenders: What Does the Data Show?, at 2, available at [http://www.uscc.gov/sites/default/files/pdf/about/commissioners/selected-articles/Howell\\_Review\\_of\\_Antitrust\\_Sentencing\\_Data.pdf](http://www.uscc.gov/sites/default/files/pdf/about/commissioners/selected-articles/Howell_Review_of_Antitrust_Sentencing_Data.pdf).

22. U.S. Sentencing Guidelines Manual §2R1.1(c) (2014).

23. Ginsburg and Wright, *supra* note 5, at 17-18.

24. *Id.* at 19.

25. *Id.* at 9.

26. *Id.*

27. See Sokol, *supra* note 3, at 201.

28. *Id.* at 203.