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High Court awards damages in first UK cartel follow-on damages judgment

On 9 October 2018 the High Court (the Court) issued a **judgment** awarding BritNed Development Ltd (BritNed) €13,009,568 in damages for overcharges resulting from a power cables cartel operated between 1999 and 2009. This is the first cartel follow-on damages judgment by the UK courts.

Background

In April 2014 the European Commission adopted a decision finding that a global power cables cartel (the Cartel) had been operated contrary to Article 101 of the Treaty on the Functioning of the European Union (TFEU). The cartelists agreed on price levels, shared markets and allocated customers, agreeing to stay outside of each other's "home territories".[1] At the time, ABB AB and ABB Ltd (together ABB) were found to have participated in the Cartel between April 2000 and October 2007, but received immunity from fines under the Commission's Leniency Notice.

During the Cartel period, BritNed and ABB entered into a supply contract under which ABB supplied cable for the 1,000-megawatt interconnector that connects the UK and Dutch electricity grids (the BritNed Interconnector). The BritNed Interconnector was constructed between 2009 and 2010. In January 2016 BritNed launched a damages claim in excess of €180 million before the Court against ABB for breach of statutory duty (breach of Article 101 TFEU and Article 53 EEA Agreement) alleging that, as a result of the Cartel, it had suffered loss and damage in connection with the supply contract.

BritNed's claims

BritNed claimed three heads of loss:

- Overcharge: BritNed paid more for the cable than it would have had there been no Cartel;

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[1] Commission fines procedures of high voltage power cables €302 million for operating a cartel.

- Lost profit: had there been no Cartel, BritNed would have invested in a higher 1,320-megawatt capacity cable which it claimed would have generated additional revenues and higher profits; and
- Compound interest: BritNed incurred higher capital costs because of the overcharge.

The Court's approach

Before deciding on the merits of the case, the Court carefully considered the definition of "overcharge", the presumption of harm in cartel damages cases, the relevance of prior bad conduct, and the nature of expert evidence provided by BritNed and ABB (the Parties). These considerations are likely to provide valuable guidance on the approach that UK courts may take in future cartel follow-on claims.

Definition of "overcharge"

ABB and BritNed disagreed on the meaning of "overcharge". ABB argued that the overcharge was the "*difference between the price actually agreed and the price that would have been agreed between ABB and BritNed had there been no Cartel*". By contrast, BritNed argued that the overcharge is the "*difference between the price actually agreed and the price that would have resulted had there been no Cartel whether the party contracting with BritNed would have been ABB or some other supplier*" (emphasis added).

The Court preferred BritNed's broader formulation, noting however that the lack of evidence would make it very difficult to determine the price that a third-party provider would offer. Mr. Justice Marcus Smith admitted that this would have a bearing on the Court's approach to the assessment of the overcharge. In determining the overcharge, he considered it not appropriate to determine what a hypothetical rival bid would have been, thus demonstrating the importance that the Court placed on evidence that can be backed up with facts.

Presumption of harm in cartel cases

The Court clearly stated that the presumption of harm in cartel cases implemented into English law by an amendment of the Competition Act 1998 pursuant to the EU Damages Directive[2] did not apply on the facts. The presumption only applies to cases arising after March 2017. The Court also dismissed BritNed's argument that the principle of effectiveness requires a presumption of harm. MJ Smith noted that if the principle of effectiveness were to require a presumption of harm, then it is difficult to see why the Competition Act 1998 had to be amended in order to establish such a presumption in English law.

Prior bad conduct

The Court refused to take into account ABB's prior involvement in other cartels noting that its propensity to participate in cartels does not "*say anything about the nature or extent of the economic benefit that ABB derived from this*".

[2] Directive 2014/104/EU.

Use of expert evidence in assessing the extent of the overcharge

The Court noted that the bespoke and unique nature of the BritNed Interconnector project meant that evidence put forth by ABB which tied closely to the facts and real data, and focused on the specific project in relation to which compensation was sought, was preferable over a model put forth by BritNed that used proxies and averages across multiple projects. In this context, MJ Smith noted that "*where there is a choice between using actual data and a proxy for that data, the former ought to be preferred, unless there is good reason for not relying on the actual data*."

The Court's judgment

The overcharge

The Court noted that the issue before it was not the general effects of the Cartel, but rather the issue of the overcharge to BritNed arising out of the specific supply contract between the Parties.

The evidence demonstrated that some people within ABB knew of the Cartel and that ABB would, as a result, face limited competition in the tendering process. However, ABB was found to have acted in "*a way unusual for a cartelist*" because the individual in charge of the bidding process was not aware of the Cartel. Consequently MJ Smith held that the "*direct costs in relation to ABB's bid for the BritNed Interconnector were honestly and competently compiled with a view to putting forward a competitive bid*". In fact, the costs of the BritNed Interconnector were found to be almost exactly in line with the equivalent figures of ABB's post-Cartel projects.

Whilst the Court did not find an overcharge resulting from the direct influence of persons aware of the Cartel and involved in the BritNed tender, the Court did establish that the existence of the Cartel resulted in "baked-in inefficiencies" and "cartel savings" which resulted in BritNed incurring overcharges.

Evidence suggested that ABB's technical solutions were designed inefficiently and used more copper than those of other suppliers. Whilst competitors may have been able to produce the same product more efficiently and at a lower cost, the effect of the Cartel was to insulate ABB from the inefficiencies in its own product. This baked-in inefficiency resulted in an overcharge of €7,516,639 to BritNed. Had there been a properly competitive market, ABB would have either lost the contract to one of its rivals or have been forced to cut its costs to remain competitive.

The Court also found that those involved in the Cartel "*derived cartel savings from their control of the allocation and supply of cable business in the market*". Cartel savings represent "*the saving to the cartelist of not having to compete*" and result in a cartelist making a greater margin on its projects. Whilst it was accepted that the cartel savings in this case were general to the Cartel and not related to any particular project, the Court found that a portion of them must be attributed to the BritNed Interconnector. On the basis of the available data, MJ Smith concluded that 1.9 per cent of the overcharge was attributable to ABB cartel savings, amounting to an additional €5,492,929 overcharge to BritNed.

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Lost profit and compound interest

The Court dismissed BritNed's claim for lost profit as evidence suggested that it would have chosen the 1,000-megawatt option over the 1,320-megawatt capacity interconnector even if there had been no Cartel. The compound interest claim failed because the BritNed Interconnector was financed 100 per cent through equity from its shareholders, and BritNed had suffered no loss as it had not been required to borrow additional money from a bank.

Next steps

On 18 October 2018 both parties won the right to challenge the Court's ruling to the Court of Appeal.

Other developments

Merger control

CMA publishes final report on its Phase 2 investigation into Vanilla Group/Washstation

On 18 May 2017 JLA New Equityco Limited (via its subsidiary Vanilla Group Limited) completed its acquisition of Washstation Limited. Both companies are active in the supply of managed laundry services. The Competition and Markets Authority (CMA) subsequently commenced a review of the transaction in October 2017 and published its **final report**, following an in-depth review, on 11 October 2018.

The CMA concluded that the transaction had resulted, or could be expected to result, in a substantial lessening of competition in the market for the provision of managed laundry services to higher education providers, and that this could lead to a degradation of the competitive offer by JLA to its customers.

In particular, the CMA found that JLA and Washstation had a combined market share of over 90 per cent in the provision of managed laundry services to higher education providers, by way of "vend share" agreements (arrangements under which the laundry services provider supplies, installs and maintains laundry machines and the customer receives commission on the revenue it generates). Washstation was JLA's closest competitor and the parties regularly bid against one another, with no other competitors providing a meaningful constraint. Both third parties and JLA's own internal documents stated that Washstation was JLA's main competitor. Further, the CMA found no evidence of recent meaningful entry or expansion in the market. The CMA therefore concluded that the transaction would result in a substantial loss of competition which could lead to higher education providers paying more for, or receiving lower quality, services.

In light of its concerns, the CMA considered that the divestiture of the entire Washstation business was proportionate and was the only possible effective remedy. It noted in particular (i) the fact the transaction concerned the first and second largest providers in the market, with competitors unable to effectively compete or expand; (ii) that divestiture was the usual approach to remedying anti-competitive

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transactions; (iii) that, according to JLA, the costs of divestiture were likely to be insignificant; and (iv) the lack of relevant customer benefits triggered by the transaction.

SAMR approves the merger of Linde and Praxair, subject to conditions

On 30 September 2018 the State Administration for Market Regulation (SAMR) conditionally **approved** the proposed merger of Linde AG (Linde) and Praxair, Inc (Praxair). Linde, listed in Germany, and Praxair, listed in the US, are both manufacturers of chemical gases. The transaction was initially notified to the Ministry of Commerce for approval on 14 August 2017. The parties withdrew and refiled the notification twice in 2018 (on 3 April 2018 and 27 September 2018), such that the total review period of over 13 months makes this the third longest review resulting in a conditional clearance.

According to SAMR's decision, the parties overlap horizontally in 56 product markets, and have a further eight vertical relationships. For certain gases, SAMR defined the geographic market by city or within a radius of 300km around a particular city. SAMR concluded that the deal would strengthen the parties' ability to control, and might eliminate or restrict competition in: the global markets for helium (combined shares of more than 40 per cent), inert rare gas mixture (combined share of 45-50 per cent), fluorine-containing rare gas mixture (combined share of 50-55 per cent), and hydrogen chloride rare gas mixture (combined share of 40-45 per cent); and the markets for liquid oxygen and liquid nitrogen in Guangdong (in which the parties have overlapping customers and are both within the top four largest players). SAMR considered, amongst other things, the potential impact on downstream semiconductor manufacturers.

To address SAMR's concerns, the parties **offered** a number of structural and behavioural remedies, as follows:

- Divestment of the parties' helium production assets with a total annual production volume of 90 million standard cubic meters;
- The transfer of helium-related customer contracts involving assets with an annual production volume of 90 million standard cubic meters with customers' consent;
- Provision of assistance to buyers in transporting the helium purchased under contract to China for processing and sale;
- Divestment of Linde's stakes in four joint ventures in Guangdong;
- The continuing supply of inert rare gas, fluorine-containing rare gas, and hydrogen chloride rare gas mixtures to Chinese customers at reasonable prices and volumes in a timely and stable manner such that:
    - the total volume of the specified gases to be supplied after the merger cannot be lower than the combined volume of specified gases supplied by the parties in 2017;
    - the merged entity must continue to supply specified gases to existing customers according to the existing contract clauses; and
    - the parties shall not set prices for contracts of specified gases at levels higher than the average of prices charged by the parties in the previous two years in China, unless the trading terms and conditions are substantially different from the existing ones, in which case the parties shall make reasonable and fair adjustments to the prices.

The divestments required by SAMR are less extensive than the ones imposed by the European Commission[3], which requires the parties to divest businesses that cover industrial, medical, specialty gases and helium. This suggests that SAMR was willing to focus only on markets in which there were substantive concerns in China.

The behavioural remedies will be in place for at least five years. SAMR's decision states that the parties may apply for lifting of the conditions five years from the date of the announcement (i.e. from 30 September 2023).

The deal has been cleared conditionally in Europe (subject to buyer approval), South Korea and the US.

General competition

CMA launches a review of the statutory audit sector

On 9 October 2018 the CMA **launched** a **market study** into the statutory audit market, to investigate concerns that it is not functioning in the interests of consumers. The announcement comes in the context of several high profile business failures, which have led to further calls for review of the statutory audit market.

In its market study, the CMA proposes to work closely with the Financial Reporting Council (responsible for the enforcement and oversight of audit regulation), which is running a parallel independent review expected to conclude by the end of 2018.

The CMA's market study will focus on three main areas that impact quality of standards and service in the sector: (i) choice and switching: whether the market currently delivers sufficient choice of auditor or whether competition takes place mostly between the big four firms; (ii) long-term resilience: whether competition between the big four auditors is sustainable in the long term or if they are "too big to fail"; and (iii) incentives: whether the fact that companies (rather than their investors) select their auditors results in a lack of incentive to produce challenging performance reviews.[4]

The CMA also proposes to consider remedies, focusing particularly on: (i) ideas for increasing competition between the big four firms, for example by separating audit and non-audit services to create audit-only firms;[5] (ii) increasing competition from non-big four firms, for example by introducing a market share cap on the big four or introducing shared or joint audits; and (iii) improving incentives, for example by removing responsibility for the appointment of auditors to shareholders or independent bodies such as sector regulators or stock exchanges.

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[3] Further details are provided in **a previous edition of this newsletter**.

[4] The CMA notes that audit is "*a service for shareholders, but is commissioned by company management", leading to a "misalignment of incentives*" (CMA Statutory audit market Invitation to comment (9 October 2018) para. 3.18).

[5] The CMA notes that 97 per cent of audits of FTSE 350 firms are undertaken by the big four firms (CMA Statutory audit market Invitation to comment (9 October 2018) para. 3.25).

The deadline for third party representations is 30 October 2018 and the CMA intends to consult on provisional reviews by the end of 2018. The statutory deadline for a market investigation reference to be made is 8 October 2019.

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