Private Antitrust Enforcement

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based on on-going work joint with
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Motivations

- 2 basic ways to deterring breaches of competition
  - With the threat of litigation by private parties
  - With enforcement by public agencies
- Even if both ways are used among all jurisdictions, there are almost no private actions in continental Europe while in the US there are 10 private actions for each action by the Public agencies
- In 2005, the EC launched a Green Paper "Damages actions for breach of the EC antitrust rules"
  - Objective: Encouraging Private Antitrust Litigation in Europe in order to enhance Europe's competitiveness

Contributions

- We model private antitrust litigation when out of court settlements are allowed
  - 80% of private cases are settled (Going to the trial is costly and time-consuming)

- We analyze the effects on litigation of:
  - The Agency's tools:
    - costs of launching a complaint
    - costs of the complete trial
    - « rewards » or damages
  - Relying only on submitted evidence or not
  - The information of the plaintiff

Literature (1)

- Breit and Elzinga (1974) are the first who have argued that a multiple damages remedy may induce private parties to "get damaged".
- Salant (1987), recognizing those perverse incentives, analyzes a model of private antitrust enforcement and states that the size of the damage multiple in treble damages imposed for antitrust violations is "neutral", and does not affect consumer welfare
- Besanko and Spulber (1990) show that this result is not robust to the introduction of asymmetric information
  - Private enforcement is similar to public enforcement. Moreover, parties do not have the possibility to settle before the trial.

Literature (2)

- McAfee, Mialon, and Mialon (2005) compare private and public enforcement of the antitrust laws with asymmetric information.
  - They show that when the court is accurate private antitrust enforcement should be encouraged while this is not the case when the court may make mistakes.
  - However, they do not consider the possibility of settlement before the trial which reduces the policy implications of those results.
- Polinsky and Che (1991) analyze private antitrust litigation when out of court settlement are allowed.
  - They show that decoupling reduces the plaintiff's incentive to sue without affecting the potential defendant's incentive to exercise care.
  - However, their analysis is made under symmetric information between the different parties and assuming perfect enforcement of the law

The Model

- The participants are the Defendant (D), the Plaintiff (P) and the Judge (J)
- The Defendant knows if he has committed a breach of competition law while, initially at least, the Plaintiff and the Judge only know that it occurred with probability (β)

The sequence of events is as follows :

- First, the Plaintiff may choose to open a case involving a fixed cost ϕ
- Pre-trial bargaining then ensues between the Plaintiff and the Defendant
  - We model this by assuming that the Plaintiff makes a single settlement offer R to the Defendant, which the Defendant may either accept or refuse.
- The trial has a fixed cost c, borne by the losing party
- At the trial the Judge observes a signal which can be interpreted as either "strong evidence" of a breach, or "weak evidence" of such breach.
- If a breach of law is established in court the Plaintiff is awarded damages F against the Defendant.

No Background Evidence

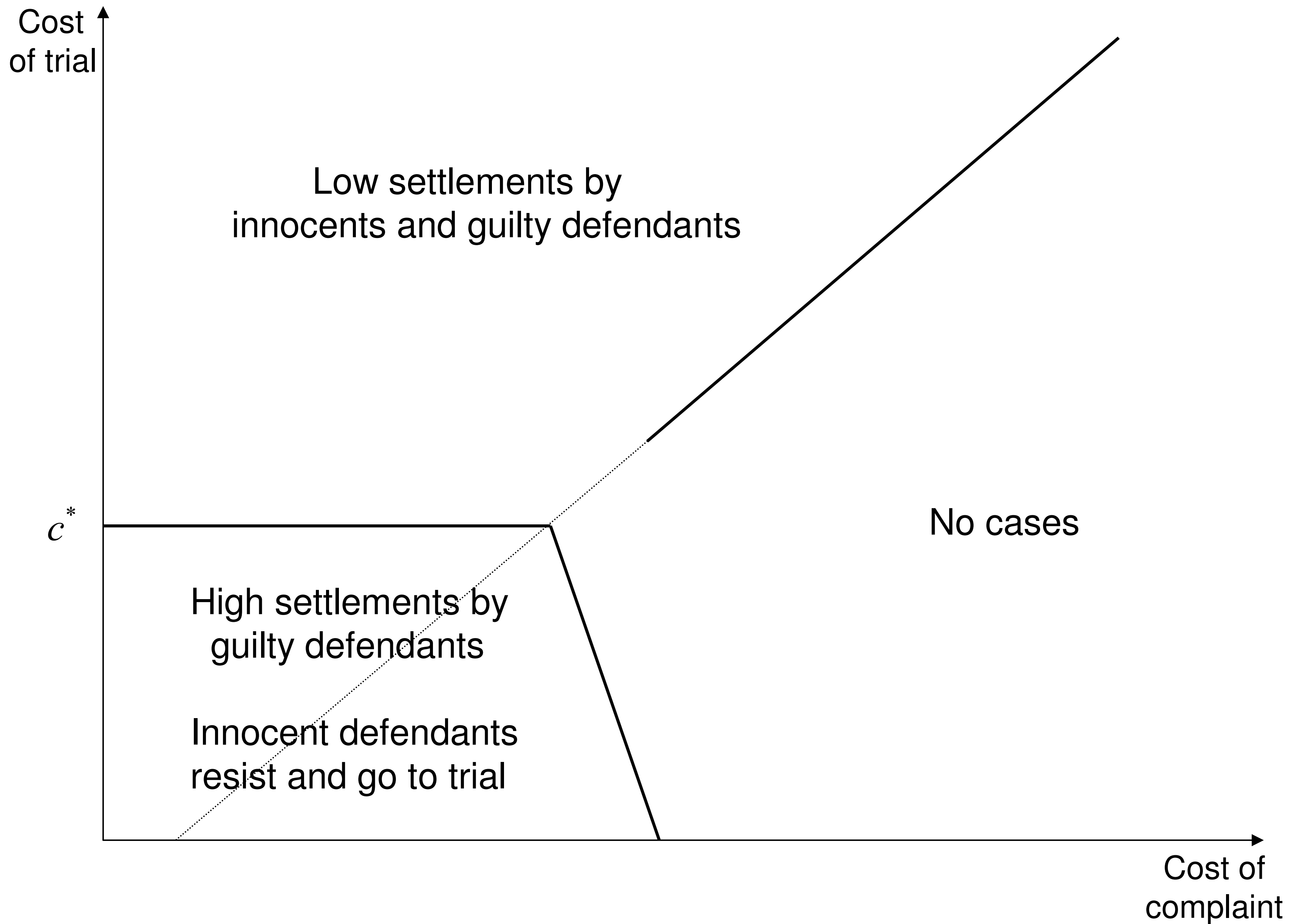
- The Judge must decide the case purely according to the signal she receives: the Defendant must be found guilty if there is strong evidence of a breach of competition law, and must otherwise be found innocent.

- In equilibrium:
  - When the costs of the complete trial are low, the Plaintiff is "aggressive", that is, demands a high settlement compensation; as a result, the Defendant settles when guilty and refuses instead to settle when innocent
  - When the costs of the complete trial are higher, the Plaintiff is less aggressive and offers a low settlement compensation, which is always accepted by the Defendant, irrespective of being guilty or innocent
  - Finally, the Plaintiff will decide to initiate a case whenever ϕ is low

Effects of encouraging private actions

- The analysis suggests that making private action more attractive will
  - Increase total cases opened
  - Increase the aggressiveness of plaintiffs in out-of-court negotiation, so innocent defendants will resist settlement and go to trial, which contributes to enhance the screening of guilty Defendants
  - Weakly increase the total number of cases brought to court
  - Increase the proportion of such cases won by defendants

Equilibrium outcome



Welfare Analysis

- Increasing rewards has an ambiguous effect on welfare
  - It increases the costs felt by both guilty and innocent defendants
  - It makes it more likely to screen out innocent from guilty defendants, by making guilty defendants pay more than innocent ones
  - ⇨ The overall welfare effect depends on whether the cost of an increased number of cases is offset by the greater differentiation in costs and outcomes for the guilty compared to the innocent defendants

- It is more desirable to lower the costs of fighting in court than to lower the costs of opening a case
  - Reducing the cost of opening a case increases the number of complaints and the costs felt by both guilty and innocent defendants
  - Reducing the cost of fighting in court reduces the costs felt by innocent defendants and makes it more likely to screen out guilty defendants

Background Evidence

- We now suppose that the Judge is fully rational and must convict the Defendant iff her posterior belief about the Defendant's guilt, based on any relevant evidence, exceeds some threshold

- Private actions are very ineffective in screening out guilty from innocent Defendants
  - Cases are either never started, or always settled for a low amount that is paid by both guilty and innocent Defendants. In neither case does a guilty Defendant end up worse off than an innocent one.
  - As a result, there is no separating equilibrium, since in such an equilibrium all guilty Defendants would have to settle while no innocent would do so; anticipating that only innocent Defendants would ever come to trial, the Judge would then never issue any convictions, which in turn induces guilty Defendants, too, to resist settlements.

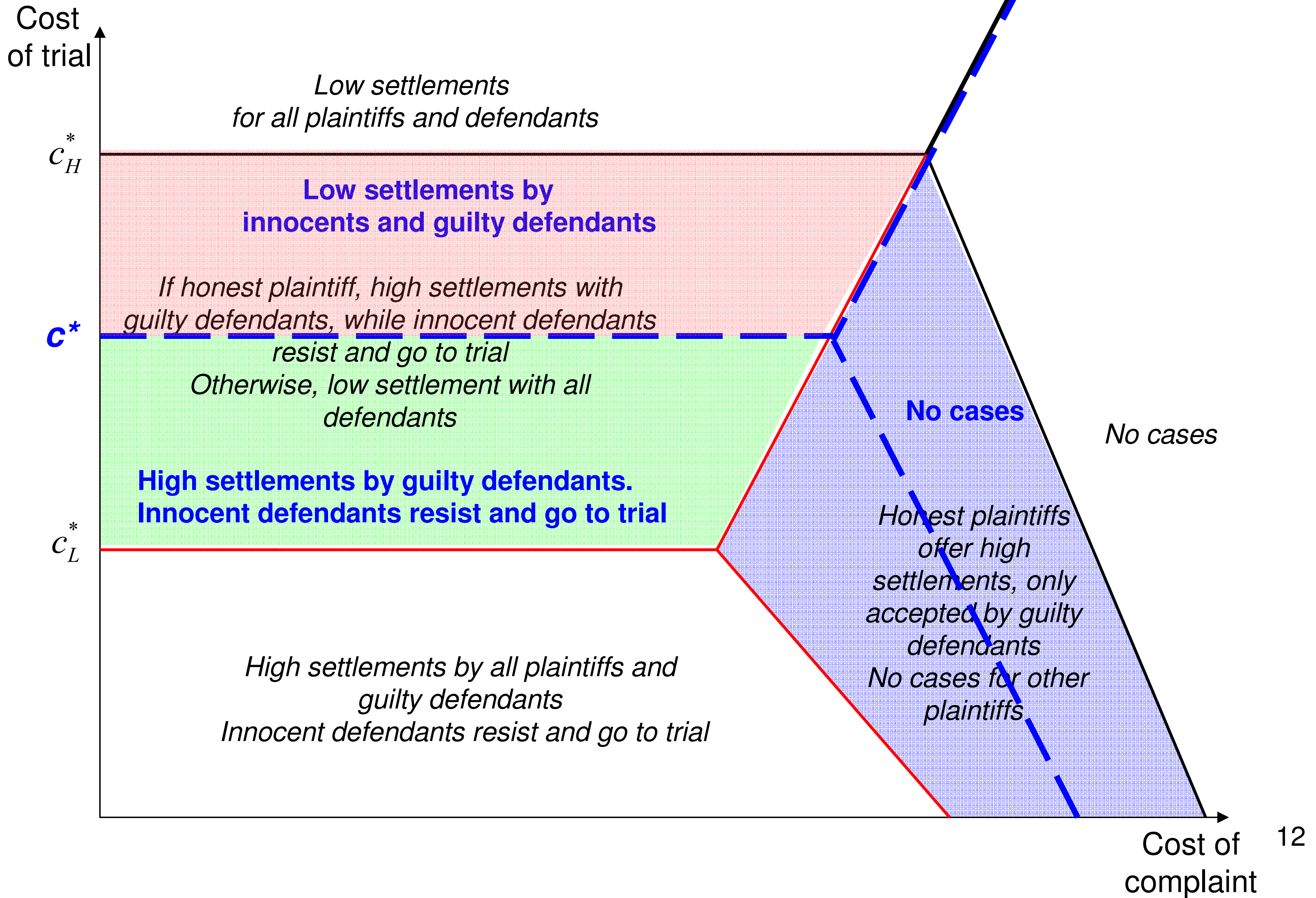
Informed Plaintiff

- We now turn to the case where the Plaintiff has some private information about whether the Defendant has committed a breach of competition law.

- We have 2 types of Plaintiffs
  - The first type has higher updated beliefs about the fact that a breach of competition law is indeed likely to have taken place and can thus be interpreted as an "honest" Plaintiff
  - The second type has higher updated beliefs and can instead be seen as an "opportunistic" Plaintiff.

- Equilibrium strategies for each type of Plaintiff take the same form as before (without any private information)

Equilibrium outcomes



Remarks

- Plaintiffs' strategies are the same in white regions.
- In the pink region, an honest Plaintiff is aggressive while an uninformed (or opportunistic) Plaintiff is not; the screening of guilty Defendants thus benefits from the Plaintiff's having some information.
- In addition, in the blue region, only an honest Plaintiff starts a case when informed, while either all Plaintiffs or none of them start cases when the Plaintiff has no information; this is again desirable because only good complaints, and not frivolous ones, are ever launched.
- In the green region, however, an opportunistic Plaintiff is not aggressive whereas she would be so in the absence of any private information; this tends to harm the screening of guilty Defendants.

Conclusion

- The effectiveness of private antitrust enforcement actions in improving overall incentives for firms to obey the law depends on their having a different impact on antitrust violators than on innocent firms
- Paradoxically, the effectiveness of the system requires innocent Defendants to be more likely than the guilty to find themselves in court.
- This in turn depends on the rules of admissible evidence:
  - If the courts are obliged to only base their decisions on submitted evidence, an equilibrium can exist which is compatible with the incentives of all parties.
  - But if the courts face no such obligation the only equilibria involve an increase in litigation with no improvement in the precision of the system as a whole.
- Reforms to facilitate private antitrust enforcement should therefore be undertaken only with very great care if they are to avoid causing more harm than good

Extensions

- We plan to consider the effect of a division of the costs in some proportion borne by the losing and winning parties respectively but also non transferable costs for each party

- Introduce the possibility of a compensation Q for a successful Defendant (beyond the reimbursement of its cost) in order to help screen out real/false claims.

- Allow the Judge to penalize Opportunistic plaintiffs for opening frivolous cases (For instance, the Judge may receive a 2nd signal on the plaintiff's information with some reliability r)