



29 February 2008

By email: cartelsbill@treasury.gov.au

Competition and Consumer Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600
Lindfield NSW 2070

Dear Sir/Madam

Discussion Paper: Criminal Penalties for Serious Cartel Conduct

Consumer Action Law Centre (**Consumer Action**) welcomes the release of the *Trade Practices Amendment (Cartel Conduct and Other Measures Bill) 2008* (the **Bill**) and the Discussion Paper on Criminal Penalties for Serious Cartel Conduct (the **Discussion Paper**).

About Consumer Action

Consumer Action is an independent, not-for-profit, campaign focused, casework and policy organisation. Consumer Action provides free legal advice and representation to vulnerable and disadvantaged consumers across Victoria, and is the largest specialist consumer legal practice in Australia. Consumer Action is also a nationally-recognised and influential policy and research body, pursuing a law reform agenda across a range of important consumer issues at a governmental level, in the media, and in the community directly.

Background

Consumer Action is pleased that the new Federal Government appears to be resolved to proceed with the introduction of a criminal regime for hardcore cartel conduct. We believe that hardcore cartels are one of the most egregious violations of competition laws and have a serious impact on consumers. In particular, such cartels can raise prices and restrict supply so that goods and services are completely unavailable for some purchasers and unnecessarily expensive for others. At the same time, being of their nature secret, consumers have no capacity to avoid their effects.

Consumer Action Law Centre
Level 7, 459 Little Collins Street
Melbourne Victoria 3000

Telephone 03 9670 5088
Facsimile 03 9629 6898

info@consumeraction.org.au
www.consumeraction.org.au

When competition laws, such as laws prohibiting cartel conduct, are considered, they should be considered in the context of the groups the laws seek to protect. In the case of cartel conduct, debate should not revolve around protection of competition as an abstract concept, but rather around protection of consumers through the promotion of competition. Cartel conduct is a problem because it distorts the operation of markets and results in consumers, and sometimes primary producers, being ripped off.

The cartel conduct involving Visy and Amcor demonstrated the impact hardcore cartels can have on consumers. Available evidence, including the institution of civil proceedings against Visy and Amcor by purchaser groups claiming multiple millions of dollars compensation, indicates that the current penalty regime does not effect the disgorgement of all profits from illegal cartel conduct and may not constitute a sufficient deterrent to induce business participants to comply with the law.

We note that, internationally, the following countries have laws providing for terms of imprisonment for cartel conduct: Canada, France, Germany, Ireland, Israel, Japan, South Korea, Mexico, Norway, Slovak Republic, the United Kingdom (**UK**) and the United States (**US**). Further, in April 2003 the Dawson Committee in its report recommended that, in light of the submissions made to it and growing overseas experience, criminal sanctions deter serious cartel behaviour and should be introduced. Since that time, we have strongly supported all proposals to implement this recommendation.

We comment, below, on particular issues which we consider important to the successful implementation of the proposed criminal and civil regime for cartel conduct:

Definition of criminal offence

The definition of the mental element required to constitute a criminal offence proposed by the Bill is likely to make successful criminal prosecution very difficult. In its current form, the requirement that the prosecution must prove that the defendant had “the intention of dishonestly obtaining a benefit” establishes a mental that would probably be so difficult for a prosecutor to prove that the deterrent effect of a criminal offence provision would be largely defeated. It should be noted that the ACCC has had difficulty successfully proving cartel conduct under the current regime (that does not require dishonest intention) and there is a strong argument that criminal enforcement would be made much harder by requiring that the prosecution prove dishonesty. This is particularly the case given a criminal prosecution of its nature also requires a higher standard of proof – beyond reasonable doubt – rather than on the balance of probabilities.

By contrast to the requirement for ‘dishonesty’, the US approach requires only that the defendant knowingly entered into the agreement.¹ The US approach does import a mental element – that of intentionally entering the agreement, but no intention as to anti-competitive effect, or subjective dishonesty.² The US approach appears pre-dominant, with several countries adopting the concept that cartel conduct is illegal without the need to prove

¹ Section 1 of the Sherman Act, 15 U.S.C 1

² United States v Brown 936 F.2d 1042, at page 1046-47 (9th Circuit 1991).

dishonesty.³ In fact, the only country that we are aware of that has a dishonesty element is the UK, and its criminal liability provision for cartel conduct is notable for the almost total lack of enforcement.⁴

Considering the difficulty the Commonwealth Director of Public Prosecution (the **CDPP**) is likely to face in proving an “intention of dishonestly obtaining a benefit” we recommend that this element of the offence be removed. We recommend the US approach be adopted. We do not agree that the proposed mental element is necessary to differentiate the criminal offence from the civil provision. The stricter procedural standards, and the differing proof requirements, of a criminal prosecution would provide a clear differentiation. Australian Competition and Consumer Commission (**ACCC**) guidelines indicating which cases will, and will not, be referred to the CDPP for criminal prosecution would provide clarity regarding what conduct will be potentially subject to criminal prosecution.

Penalties for criminal conduct

The importance of imprisonment as a deterrent for cartel conduct is widely acknowledged. The threat of imprisonment is recognised as a strong deterrent against the formation of cartels.⁵

We believe, however, that the proposed maximum term of imprisonment of 5 years for individuals guilty of cartel conduct is not sufficiently long and should be increased to a maximum term of imprisonment of 10 years. Cartel conduct is very hard to detect and successfully prosecute (and will be even harder if the currently proposed mental element is retained). By their nature, cartels are sophisticated organisations that operate secretly. Only a small minority of cartels are ever ‘cracked’.⁶ Considering this, the individuals who participate in the creation and management of cartels are unlikely to be prosecuted. Further, a 5 year maximum prison term often results in an offender serving no or minimal jail time.

Already, in corporate law, a number of individuals who have been convicted for offences that carry a maximum five year jail term have been given a trivial prison term, or no term of imprisonment at all.⁷ Many cartel participants will be aware of this, and clearly while the threat of any prison term will be a deterrent, the knowledge that corporate offenders (who

³ For instance, section 6 of the Irish *Competition Act 2001*, contains a presumption that agreements have an anti-competitive object, which is all that is required.

⁴ Andrew Bell, ‘Criminal Cartel discussion paper marks major changes to Trade Practices law’, *Competition and Consumer Law Update*, Deacons, 1st Ed 2008. Available at: http://www.deacons.com.au/UploadedContent/NewsPDFs/CC_03_0208.html

⁵ Sjoerd Arlman, *Crime But No Punishment: An empirical study of the EU’s 1996 Leniency Notice and cartel fines in article 81 proceedings*, draft of 26 August 2005, page 12. Available at: http://www.encore.nl/publications/crime%20but%20no%20punishment_arlman.pdf

⁶ Because of the secretive nature of cartels, there are not currently reliable data on the percentage of cartels that are detected and subjected to prosecution. Nonetheless, it has been observed that based on the current low levels of detection combined with inadequate enforcement methods means that cartel conduct such as price fixing is rational conduct in many Asian jurisdictions. See: John Conner, *Global Antitrust Prosecutions of International Cartels: Focus on Asia*, Purdue University, delivered to Asian Law and Economics Association August 16-17 2007, Taipei, Taiwan, page 48.

⁷ For example: *R v Howard* [2003] NSWSC 1248 (23 December 2003) involved a case in which the defendant was convicted of two breaches of section 184 of the *Corporations Act (Cth) 2001* by dishonestly using his position with the intention of gaining an advantage for himself and others, an offence carrying a maximum 5 year jail term. The defendant was not jailed.

usually have no criminal record to constitute an aggravating circumstance in sentencing) will often serve little or no prison time will blunt this deterrent effect.

For crimes that have a low level of detection and successful prosecution (such as cartel conduct) it is necessary to impose high penalties (in this context, imprisonment) to achieve an effective deterrent.⁸ The optimal prison term is influenced by the risk attitude of the likely criminal participants.

Cartel participants are usually high-level corporate officers, a group that has been identified as being very risk averse.⁹ This risk-aversion, combined with the well recognised difficulty in detecting cartels, means that the most efficient deterrence system would impose a high penalty on the few individuals who are convicted of criminal cartel conduct. The argument for a high maximum prison term is supported by research into general deterrence that shows that, for risk averse individuals, the economically optimal enforcement approach is to combine a low risk of prosecution and conviction with a high penalty upon conviction.¹⁰

Accordingly, an economically optimal enforcement approach would combine the existing low chance of detection, prosecution and conviction for cartel conduct with a harsh penalty upon conviction to maximise the general deterrence effect.¹¹ We believe that a 10 year maximum prison term is a suitable prison term to achieve general deterrence, and is consistent with existing prison terms for other white-collar Commonwealth offences such as bribery.¹² A 10 year maximum prison term would also be consistent with the non-violent crime of theft under the *Crimes Act 1958 (Vic)*.¹³

We are also concerned that the fines that can be imposed upon a cartel offender under the criminal provisions are too low. In particular, for individuals who are attempting to contravene or are involved in a contravention of a cartel offence provision, the maximum fine is \$220,000 (which can occur in addition to prison time). This amount is at odds with the maximum civil penalty of \$500,000 for contravention of the new and existing civil penalty prohibitions for cartel conduct, and breaches of other provisions under Part IV of the TPA. Further it is out of step with international fines, which include US \$1 million, Canada \$10 million and in the UK it is unlimited. We think the amount should be reviewed to be brought in line with international standards.

Civil penalties and banning orders

The inclusion of civil penalties for cartel conduct is appropriate as it allows balanced regulation following an enforcement pyramid approach, and an effective enforcement response to situations where wrongful conduct is insufficiently serious to warrant criminal prosecution (or where, because of its higher procedural and standard of proof requirements,

⁸ James Mayanja, 'Promoting Enhanced Enforcement of Directors' Fiduciary Obligations: The Promise of Public Law Sanctions', (2007) 20 *Australian Journal of Corporate Law* 157, pages 175-176.

⁹ Stephen Yoder, 'Criminal Sanctions for Corporate Illegality', (1978) 69 *The Journal of Criminal Law and Criminology* 40, page 45.

¹⁰ *Ibid.*

¹¹ It would be extremely difficult and costly (if not impossible at present) to increase cartel detection and conviction rates so that cartel participants were likely to be prosecuted. Given this, increasing prison terms is the only effect mechanism available to maximise deterrence.

¹² *Commonwealth Criminal Code 1995* section 141.1.

¹³ Section 74.

criminal conviction is unlikely). Following an enforcement pyramid approach, it is desirable that there be a level of enforcement below criminal prosecution that still has a deterrent effect. Civil penalties, with their easier to satisfy standards of proof, fit this role.

We note that the new civil penalty prohibitions will not replace the existing civil penalty prohibitions under section 45 of the TPA (although section 45A relating to price fixing will be removed). We are concerned that there is some confusion about how the new civil penalty prohibitions will operate in conjunction with section 45.¹⁴ It is our view that a more cogent approach would be for section 45 to target cartels generally (contracts, arrangements or understandings that contain an exclusionary provision or have the purpose, effect or likely effect of substantially lessening competition) and for the new civil penalty prohibitions to target certain types of 'hard-core cartels' (being price-fixing, output restriction, market allocation and bid rigging). The proposed criminal cartel offence could then apply to the latter types of conduct and prosecution pursued where the conduct was viewed as serious enough by the ACCC and CDPP.

However, as outlined above, the effectiveness of pecuniary penalties as a deterrent effect for big business cartel conduct is questionable, and hence we recommend that a management banning order be one of the civil penalties available to courts in relation to cartel conduct. Under section 206C(1) of the *Corporations Act 2001* (Cth), the Court can order that a person be disqualified from managing a corporation if they have been found to have breached a civil penalty provision. It would be entirely appropriate for such a banning order to be available in the present context of cartel conduct. Giving the ACCC the power to apply to court to have a participant in a cartel banned from managing a corporation would provide another layer of deterrent, and would be particularly useful in circumstances where a criminal prosecution is not warranted or cannot be achieved, but where a fine would not be a sufficient penalty. It worth noting that the Productivity Commission in its Review of Australia's Consumer Policy Framework recommended banning orders be made available as a possible penalty for breach of consumer protection laws.¹⁵

Telephone interceptions

Consumer Action has recommended that the maximum term of imprisonment for criminal cartel conduct be set at 10 years. If this recommendation were to be implemented, the Australian Federal Police (the **AFP**) would be able to obtain a TI warrant by Court order to assist an ASIC investigation. 10 years is obviously over the 7 year maximum penalty that triggers the right for law enforcement to apply for a TI warrant. Facilitating the obtaining of TI warrants is no reason for making the maximum penalty 10 years, however it would be one minor benefit that would result from this approach.

Even if the maximum prison term for criminal cartel conduct were set at less than 7 years, in our view it is appropriate for a TI warrant to be available. Although intercepting telephone

¹⁴ Caron Beaton-Wells and Brent Fisse, 'Criminalising Serious Cartel Conduct: Issues of Law and Policy' *Paper presented at the University of Melbourne*, 18 February 2008.

¹⁵ Productivity Commission, *Review of Australia's consumer Policy Framework*, November 2007, Volume 2, page 190.

conversations is an invasion of privacy,¹⁶ giving the AFP the power to obtain a TI warrant is justified for two reasons.¹⁷ Firstly, the social harm that results from cartel conduct is enormous in economic and consumer welfare terms. Secondly, cartel conduct is generally very hard to identify and prove. Cartel participants conduct themselves in secret, often taking significant steps to cover their actions. Accordingly, TI warrants are justified because of the difficulty of gaining evidence in cartel conduct cases, and because such warrants an important potential source of evidence available.

While it may be the case, looking particularly at the US jurisdiction, that most convictions are obtained because whistleblowers take advantage of the amnesty system (and therefore the most successful covert surveillance device is often a 'wire' worn by the whistleblower), experience demonstrates that cartel communication is also likely to take place over the phone. For example, in the *Geelong Petrol* case, the ACCC failed to convince the Court that a civil contravention of the cartel conduct prohibition had occurred.¹⁸ A primary piece of evidence the ACCC used was detailed analysis of call records between the petrol station owners. By this, the ACCC sought to show that the pattern of telephone calls evidence price fixing. The ACCC was not successful, however had they been able to intercept and record the telephone conversations between the petrol station owners the outcome could have been very different.

The *Geelong Petrol* case suggests that in many circumstances telephone will be the primary means of communication between competitors within an industry, and that in the absence of interception and recording of telephone calls these calls may serve little evidential benefit in securing conviction.

ACCC/CDPP enforcement policy and the role of lenience/immunity

We make the following general observations regarding the ACCC and CDPP's immunity policies:

- We agree that immunity policy has been crucial to the effectiveness of the ACCC's enforcement policy generally;
- We note that corporate penalties for cartel conduct have fallen over recent years and we are concerned at the implications of this for a criminal penalty regime;
- The current ACCC enforcement policy appears to be focused on obtaining negotiated outcomes and we are concerned of the implications of this for a criminal penalty regime;
- The ability for third parties to access documents held by the ACCC through the discovery process where a cartel participant has cooperated with the ACCC has been confirmed in a recent case¹⁹ that may, to some extent, undermine any immunity policy.

¹⁶ Which many view as a fundamental human right. For instance, protection from arbitrary interference with privacy is protected in section 13 of the *Charter of Human Rights and Responsibilities Act (Vic) 2006*.

¹⁷ Note also, many argue human rights can be limited in particular circumstances: see section 7 of the *Charter of Human Rights and Responsibilities Act (Vic) 2006*.

¹⁸ *ASIC v v Leahy Petroleum Pty Ltd* [2007] FCA 794 (29 May 2007).

¹⁹ *Cadbury Schweppes Pty Ltd (ACN 004 551 473) v Amcor Limited (ACN 000 017 372)* [2008] FCA 88 (19 February 2008). The court allowed the release of two out of three categories of documents that the ACCC held that related to Amcor, and that Cadbury sought to use against Amcor.

An immunity system that indemnifies whistleblowers from civil and criminal proceedings has been shown to be very successful in overseas jurisdictions such as the US.²⁰ A system of absolute immunity for the individual who is ‘first past the post’ (that is, the first to break ranks and reveal the cartel conduct to the ACCC) should be implemented. This system of immunity should be explicit and consistent, and provide absolute immunity from civil and criminal liability for the first cartel participant who cooperates with the regulators. Under this system, both the ACCC and the CDPP do not retain discretion to prosecute the cartel participant who is the first to cooperate (that is, immunity should be absolute and not discretionary).

In its current draft form, the Memorandum of Understanding (**MOU**) between the ACCC and the CDPP does not contain sufficient clarity about how the CDPP will exercise its discretion to grant immunity to provide the certainty (for cartel participants) needed for such a scheme to work. An immunity program should be agreed to between the ACCC and the CDPP that gives absolute immunity for the first cartel participant to cooperate with prosecutors – this means immunity should be automatic and not discretionary. This is consistent with the US approach to immunity, which is widely accepted as a major contributor to its highly successful cartel prosecution results.²¹

Failure to implement an optimal immunity system will make the difficult job of obtaining a criminal conviction even more difficult. An immunity policy that absolutely protects the first whistleblower will make it much easier for the ACCC to gather the evidence necessary for the CDPP to secure a conviction.

Compensating consumers

As pointed out above, cartel conduct, by damaging competition, harms consumers. While inflated prices may be absorbed to some extent by businesses along the supply chain before final consumption, inflated prices will typically be passed-on to the least powerful party (that is individual consumers).

Individual consumers are usually not capable of initiating legal proceedings to recover their losses. This is due to the cost of legal representation, and the fact that frequently the amount of harm suffered by consumers as individuals will be too small to warrant legal proceedings.

Class action proceedings in their current form will also do little to assist many individual consumers. In many instances, it will be possible to quantify consumer loss generally, but impossible to individualise that loss to determine how much loss individual consumers have suffered. The recent *Visy* case illustrates the problem, with large businesses along the

²⁰ Thomas Barnett, Assistant Attorney General, Antitrust Division, US Department of Justice, *Criminal Enforcement of Antitrust Laws: The US Model*, address presented to the Fordham Competition Law Institute’s Annual Conference on International Antitrust Law and Policy, New York, September 14, 2006.

²¹ Julian Joshua, & Donald Klawiter., The UK “Criminalisation” Initiative: Step Forward or Another Complication?, Antitrust, Summer 2002, page 11. See also Makan, Delrahim (Deputy Assistant Attorney General, Antitrust Division, US Department of Justice), *The Basics of An Effective Anti-Cartel Enforcement Program*, address to the Seoul Competition Forum Seoul, Republic of Korea April 20, 2004, that claims absolute immunity is a necessary sacrifice for a vigorous prosecution system.

supply chain taking legal proceedings, but individual consumers buying retail products at inflated prices having no prospect of doing likewise. Even where small consumers can join class action proceedings to recover losses, their ability to do so will often depend upon the business decisions of litigation funders, whether they be plaintiff law firms or independent entities. Due to the significant cost risks involved, independent consumer legal services like Consumer Action cannot easily launch representative proceedings on behalf of consumers at large.

The regulator, also, has little power to recover refunds on behalf of affected consumers upon breaches of the TPA outside proceedings in which all affected consumers are named. The cases of *Medibank Private Ltd v Cassidy*²² and *ACCC v Danoz Direct*²³ demonstrate that the regulator is hamstrung to do so. One solution to this problem would be to allow the ACCC to make a civil claim for compensation on behalf of consumers.²⁴ This would likely require the Court to be empowered to make a *cy pres* order.

Cy pres orders are useful in situations where an individual or corporation will make a windfall profit because the people from whom they have wrongfully benefited cannot be identified. The proceeds of *cy pres* orders would be paid toward a purpose designed to benefit the class of people who have suffered loss (for example, if cartel conduct by casino and gaming participants were proven, a *cy pres* order could require the cartelists to pay funds to organisations that assist problem gamblers).

In the case of cartel conduct, cartel participants, and the companies for whom they work, make windfall profits at the ultimate expense consumers. It may be difficult or impossible to identify consumers who have suffered loss for a number of reasons: the value of consumer purchases may have been so low that consumers would not record these purchases; the product that was cartelised may have been converted into other products before retail sale and it is therefore impossible to know exactly which final products it has effected and what price difference this has made for those final products; there may be specific evidence of wrongful profit by the cartel participants but no adequate evidence of which consumers this profit was extracted from.

A system that allows the court discretion to make a *cy pres* order is important in that it promotes general deterrence against cartel conduct. Any order that makes the cartel participants disgorge their wrongful gains acts as a deterrent. While criminal sanctions are the key to maximising general deterrence against cartel conduct, civil proceedings can support this goal.

²² (2002) 124 FCR 40.

²³ [2003] FCA 1580 (287 August 2003).

²⁴ Another novel approach, advocated by Frank Zumbo, that would assist small business owners, is giving Federal Court judges in proceedings brought by the ACCC the power to make a 'class compensation order' whereby third parties would have the option of presenting a claim to a court appointed assessor within a specified period of time. See Zumbo, Frank, *More classy way to recover loss*, Australian Financial Review, 26 February 2008, page 21.

Defences and exceptions

A number of defences and exceptions may be necessary to ensure that conduct that Parliament does not intend to result in criminal liability does not so result. One clear example is joint venture agreements.

However, the exclusion of liability for a contract, arrangement or understanding between bodies corporate that are related to each other is problematic. It is noteworthy that the *Trade Practices Legislation Amendment Act (No.2) 2006* exempted related bodies corporate from third line forcing prohibitions. This amendment, under the previous Government, is unfortunate and retrograde.

In relation to the cartel conduct offence, we are concerned at the potential scope for a loophole in relation to the defence for “bodies corporate that are related to each other”. Clearly, the content of a specific definition of “bodies corporate that are related to each other” will be critical in determining whether this defence creates an unjustifiably large loophole. We take the view that extending the defence any further than to wholly owned subsidiaries is a recipe for a loophole that will undermine the object of the legislation.

Importance of enforcement

Effective enforcement is important for the success of competition laws. In relation to criminal cartel conduct, a number of specific aspects of enforcement are important to the law's success.

Firstly, specific and dedicated funding directed to the prosecution of criminal cartel offences is required.

Secondly, significant media coverage of the laying of any charges or the finding of any guilt should be encouraged by the regulator.

Thirdly, as modern business has become increasingly globalised, the largest modern cartels are often also global organisations. It is therefore important that in pursuing its enforcement the ACCC continue to collaborate and cooperate with overseas regulators in ‘cracking’ international cartels. To this end, it should be noted that international cartels cause more economic harm than national cartels as the amount they overcharge for their products is typically substantially higher than the overcharge of national cartels.

Fourthly, effective enforcement will only be possible if there is a clear and transparent immunity regime in Australia that grants immunity to the first cartel participant who cooperates with the regulator. If the ACCC is to be able to effectively work with international regulators (such as those in the US, Canada and Europe) it will need to be able to have an effective immunity regime to work with. For instance, a particular company in a cartel may wish to cooperate with prosecutors, but may also wish to ensure its employees are immune from criminal liability in all jurisdictions (particularly if it is these employees themselves who are making the decision about whether or not to cooperate with prosecutors).

Finally, we believe the ACCC should develop guidelines which set out its enforcement approach. These guidelines should cover the following:

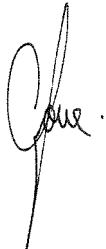
- the types of action available to the regulator;
- the principles behind each of these actions;
- the criteria involved in the decision to pursue one or more of these actions; and
- the regulator's relationship with other regulators and enforcement agencies.

We note that this is in accordance with a recommendation from the Australian Law Reform Commission.²⁵

Should you have any questions in relation to this submission please contact Gerard Brody on (03) 9670 5088.

Yours sincerely

CONSUMER ACTION LAW CENTRE

A handwritten signature in black ink, appearing to read 'Catriona Lowe', with a large loop at the start and a long vertical stroke at the end.

Catriona Lowe
Co-CEO

²⁵ Australian Law Reform Commission, *ALRC calls for more transparent, consistent and 'principled' regulation*, Media release of 19 March 2003. <http://www.alrc.gov.au/media/2003/mr0319.htm>