SWEDISH KONKURRENSVERKET

CONFERENCE ON THE PROS AND CONS OF COUNTERFACTUALS

STOCKHOLM 6 DECEMBER 2013

PREDICTING THE PAST CONSTRUCTING THE COUNTERFACTUAL IN ANTITRUST DAMAGES CLAIMS

Dame Vivien Rose DBE
Justice of the High Court, Chancery Division

1. There have been many conferences in recent years devoted to analysing why the long hoped for rush of claimants seeking damages for loss caused by antitrust infringements is yet to materialise. One issue always covered is whether the infringement decision – either of the EU or the domestic enforcement authority - is binding on the court deciding any follow-on damages claim. It is generally thought that in jurisdictions where the infringement decision does have binding force, this is a great help to the claimant. After all, the only thing that the claimant then has to do is prove causation and quantum. What could be simpler?

2. In fact this is often not at all simple and the reason why that is so, is often to do with the difficulty of establishing the correct counterfactual which the court will use to assess causation and quantum. To establish loss, the Claimant must show what would have happened if the illegality had not taken place.

3. In examining the pros and cons of constructing a counterfactual I will refer to four recent cases. Three of them were follow-on damages claims in the Competition Appeal Tribunal. All three concerned findings of abuse of a dominant position. The other is a case which heard recently in the High Court in London. This fourth case was not an anti-trust case but a *Francovich* damages claim. However, it raised many of the same questions that are raised in anti-trust damages claims and so can serve as a useful analogy.

4. The four cases are:

    - *Enron Coal* [1] The Defendant, EWS, provided coal haulage services to the claimant, ECSL. The Office of Rail Regulation had found that EWS was dominant and had pursued, without objective justification, selective and discriminatory pricing practices that had placed ECSL at a competitive disadvantage. ECSL alleged that EWS' abusive conduct caused ECSL to lose a tender for the haulage of coal by rail to power stations operated by Edison Mission Energy Limited. ECLS also claimed that it had lost the opportunity to secure a four year contract to supply coal to one of those power stations, Ferrybridge C. The issue of causation

[1] *Enron Coal Services Limited (in liquidation) v English Welsh & Scottish Railway Limited* [2009] CAT 36

was at the centre of the litigation. The Tribunal held that EWS has not proved that any loss had been suffered as a result of the infringement. No damages were awarded.

- *2 Travel* [2] The claim was based on a finding by the Office of Fair Trading that the Defendant, Cardiff Bus, had abused its dominant position by engaging in predatory conduct aim at causing a new market entrant, 2 Travel, to exit the market. 2 Travel had gone into liquidation by the date of the claim. 2 Travel's claim covered various broad heads: (i) loss of profits; (ii) loss of a capital asset, namely the business of 2 Travel as a going concern; (iii) loss of a commercial opportunity, namely the ability to benefit from the increase in value and development potential of certain land in Swansea; (iv) wasted staff and management time expended by 2 Travel during the infringement period; and (v) costs relating to 2 Travel's liquidation. The Tribunal awarded damages to 2 Travel in respect of its claim for lost profits in the amount of £33,818.79. The Tribunal rejected 2 Travel's claims for loss of a capital asset, loss of a commercial opportunity, wasted staff and management time and liquidation costs.
- *Albion Water* [3] This was a claim for damages brought by Albion Water Limited ("Albion") against Dŵr Cymru Cyfyngedig ("Dŵr Cymru") based on the finding, made by a differently constituted panel of the Tribunal that the price that at which Dŵr Cymru was prepared to offer Albion a common carriage service to carry water through its pipes (the "First Access Price") amounted to an abuse by Dŵr Cymru of its dominant position. The abuse found was both a margin squeeze and excessive pricing. Albion's claim for damages asserted that if Dŵr Cymru had offered a lawful price for common carriage, rather than the abusive price, Albion would have been able to supply its customer, Shotton Paper, on the basis of common carriage, which would have been more profitable than the existing arrangements. Albion also alleged that as a result of the infringement, Albion had lost the chance to win a potentially lucrative contract to supply another business, Corus Shotton. The Tribunal upheld both claims and awarded Albion damages in the amount of £1.7 million overall.
- *Recall Services v Department for Culture Media and Sport* [4] This was a claim for *Francovich* damages arising out of restrictions imposed by the Government on the use of a particular piece of telecoms equipment. The companies who provided services using that equipment claimed that their businesses had been destroyed by the restriction and they had lost substantial on-going profits. The Court found that there had been a breach of EU law in failing properly to implement the Telecoms Authorisation Directive, although the breach was considerably less extensive than the Claimants had alleged. However, the second *Francovich* condition was not

[2] *2 Travel Group PLC (in liquidation) v Cardiff City Transport Services Limited* [2012] CAT 19
[3] *Albion Water Limited v Dŵr Cymru Cyfyngedig* [2013] CAT 6
[4] *Recall Support Services Ltd & Ors v Secretary of State for Culture, Media and Sport* [2013] EWHC 3091 (Ch)

satisfied in that the breach did not constitute a serious and manifest disregard of the State's obligations. The Court found that causation lad been established.

But for…. what?

5. The counterfactual is often referred to as the 'but for' world. This raises the question, in what way should the world that the court is constructing to assess causation and quantum be different from the actual world as it played out over the years after the infringement – the years during which the claimants say they have suffered loss?

6. The simple answer is 'but for the illegal conduct'. What the court has to strip out is the infringement itself. This led to an interesting issue in the *Albion* case. There the infringement was an abusively high price offered to a competitor to make use of a water pipe infrastructure owned by the dominant water company. The claimant competitor alleged that because of the excessive price offered for access to the infrastructure, it had to adopt a less profitable business model for many years than the business model it wanted to adopt making use of common carriage.

7. To find out whether there had been any loss of profit, the Tribunal had to construct a counterfactual as if an abusive price had not been offered. This raised the question what price should be included in that counterfactual for access to the pipe? The abusive price which made the service unattractive was 23.2 pence per cubic metre of water carried. In the counterfactual we had to decide, what *should* the price be?

8. The dominant company - the defendant in the proceedings – argued that the court's task is to strip out the illegal conduct. So the price that should be used in the counterfactual is the highest price that the dominant company could have charged without actually committing an infringement. This could be substantially above a reasonable price – certainly substantially above cost – because of the two fold test set out by the European Court of Justice in Case 27/76 *United Brands v Commission* [1978] ECR 207. The Tribunal would, according to the Defendant, have to work out what is the highest margin above the cost price that Dŵr Cymru could have charged and, then, assess what is the maximum value that Albion would have placed on the service. That would give the maximum price that Dŵr Cymru could lawfully have charged without committing an abuse. That should be the counterfactual price.

9. The Tribunal rejected this as a matter of principle and as being entirely impractical to apply. Albion referred the Tribunal to the case of *Banque Bruxelles v Eagle Star* [1997] A.C. 191. In that case the House of Lords considered the issue of counterfactuals in respect of a negligent valuation. Their Lordships held that if the figure put forward by the valuer is found to be wrong, the correct figure for the purposes of calculating the loss caused is the *average* one which a non-negligent valuation would have produced. At page 221, Lord Hoffmann said:

> 'I must notice an argument advanced by the defendants concerning the calculation of damages. <u>They say that the damage falling within the scope of the duty should not be the</u>

> loss which flows from the valuation having been in excess of the true value but should be limited to the excess over the highest valuation which would not have been negligent. This seems to me to confuse the standard of care with the question of the damage which falls within the scope of the duty. The valuer is not liable unless he is negligent. … But once the valuer has been found to have been negligent, the loss for which he is responsible is that which has been caused by the valuation being wrong. For this purpose the court must form a view as to what a correct valuation would have been. This means the figure which it considers most likely that a reasonable valuer, using the information available at the relevant date, would have put forward as the amount which the property was most likely to fetch if sold upon the open market. While it is true that there would have been a range of figures which the reasonable valuer might have put forward, the figure most likely to have been put forward would have been the mean figure of that range. There is no basis for calculating damages upon the basis that it would have been a figure at one or other extreme of the range. Either of these would have been less likely than the mean.' (emphasis added)

10. The Tribunal held that the same principle applied by analogy in the *Albion* case. There was a range of lawful access prices that Dŵr Cymru could have offered and the appropriate price to include in the counterfactual was a figure in the middle of that range. The counterfactual must be based on an assumption that Dŵr Cymru would have offered a reasonable access price, rather than an access price which is the highest it could lawfully have charged. The Tribunal considered that to apply the test suggested by the Defendant would require the court in the follow-on damages to re-do much of the work that had been done by the court or institution which had made the finding of infringement. It is rare that an infringement decision will identify with precision where the dividing line between lawful and unlawful conduct lay. In the infringement decision that was the foundation for the follow-on damages claim in *Albion*, the Tribunal had arrived at three figures representing a reasonable cost on the basis of three different cost methodologies. Since the First Access Price had been substantially in excess of all of these, the court had found the infringement. The Tribunal in the damages claim took the average of the results of the three different cost methodologies as the reasonable price for the counterfactual and increased it by inflation over the period for which loss was claimed.

11. Interestingly this was not an issue raised in the *2 Travel* case. There the abuse had been a predatory pricing abuse where the dominant bus company had expelled a new entrant out from the market by starting up a very cheap service. It ran its buses at frequencies which resulted in its buses picking up passengers just before the new entrant's buses came along. It was accepted by the parties in that case that the correct counterfactual was that no new bus service had been launched. One can see how difficult it would have been if the court had been required to imagine a new bus service launched by the dominant company where the price was just high enough and the frequency or timing of the buses was just different enough to escape the charge of being predatory before considering what the effect of such a service on the claimant's business would have been.

Assumptions about the possible illegal behaviour of others

12. Allied to the question of what illegality is stripped out of the counterfactual is the question of what assumptions the court should or could make about whether undertakings will abide by the law in the counterfactual world. More generally, can the court assume that undertakings would have acted reasonably rather than in an obstructive manner? It is often the case that the counterfactual has to posit behaviour not just of the defendant but of a third party.

13. There are a number of ways the court might approach this. The first, which is deeply unattractive, is to say that the court must conduct 'a trial within a trial' – that is, conduct a trial as if the putative unlawful conduct had taken place and come to a conclusion as to whether that conduct would have been abusive.

14. Such an approach clearly leads to problems. The first problem is that it risks considerably lengthening the trial of the damages claim and bringing in many complex issues that do not otherwise arise in the case. For example where the unlawful conduct is alleged to be an abuse by a third party, what is the relevant market that the third party is active in or what price would be abusive. The second problem is that no such trial of a hypothetical abuse can be really accurate. All abuse cases depend on their actual facts, for example whether there is an objective justification for the refusal to supply this particular customer even if the third party is assumed to be dominant and even if it is assumed that generally speaking a refusal to supply would be an abuse. Do you assume, against the dominant third party that the claimant had always paid their bills on time?

15. What is the alternative approach? One choice is to look at contemporary documents from the third party and see what view they took as to their own obligations. For example if there were internal documents from the relevant period in which senior executives acknowledge that there is a risk that they might be held to be dominant at some time in the future and concluding that the safest course is to price on the basis that they are dominant, that might help the court decide that in the counterfactual world the third party would have supplied or would have quoted a reasonable price.

16. Similarly if they had received legal advice on that or some other issue indicating that they were or might well be considered dominant, then that might help the court decide how they are likely to have behaved.

17. But again there are problems with this. First you might not have access to this internal documentation if the third party is not taking part in the trial and is not providing witness evidence to the court. Secondly, the court might be less comfortable if the internal documentation available showed that the senior management, while acknowledging that it might be dominant, concluded that it should take the risk of charging as high a price as possible until challenged and then dispute any such challenge as vigorously as possible. It seems somehow unsavoury for a court to take that kind of behaviour into account when constructing the counterfactual.

18. It may help to describe some examples as to how this has been considered in the cases.

19. In *Albion* one important aspect of the counterfactual was the question of what the Claimant Albion would have had to pay for the water if it had entered into a common carriage arrangement with the defendant. The water would have been bought from United Utilities ("UU"). The Tribunal knew that UU was charging its other customer a very low price for the water. But the evidence from UU was that this was a historic low price that they were tied to in a very old contract; that price did not cover their long run marginal costs and so they would have charged at least three times as much in the counterfactual world.

20. The Tribunal approached the matter by considering first the commercial positions of the different parties and their relative bargaining positions. We then looked at whether there was any evidence to support the contention that the low price they were in fact charging their other client did not cover their costs and found that there was no such evidence – it appeared to us clear that the price was reasonable. We held that the correct counterfactual price for the water was lower price.

21. In *Recall Support Services* the Government argued that the claimants would not have been able to develop a business using the piece of telecoms equipment in issue because to do so, they needed to buy SIM cards from the mobile network operators. There was evidence that the MNOs did not want that equipment attached to their networks and that they would have refused to supply SIM cards. The Government asserted that the scale of the losses claimed was much too high because it did not take account of the fact that the MNOs would have limited the number of SIM cards available. This raised the question whether it would have been an abuse of a dominant position for the MNOs to refuse to supply the claimant with as many SIM cards as they wanted to operate their service – in other words, could the claimants have forced the MNOs to supply them with the SIM cards they needed?

22. As with the *Albion* case the parties differed in the approach that they said the court should adopt. The Defendants said that the court had to be satisfied that a claim for abuse of dominance would have succeeded and that the MNOs would have been forced to supply the Gateway operators with SIM cards. I held that this was not the correct approach. The court has to make an assessment not of how the MNOs **should** have behaved in the counterfactual world (that is the world where the statutory restriction on use had been lifted) but how they **would** have behaved. An analysis of the legal position showed that there would have been many complex issues raised by any litigation in which it was alleged that refusal to supply the SIM cards was unlawful. There would have been issues about the definition of the relevant market and objective justification. In many respects any court deciding such a case would have had to break new ground in finding the conduct to be abusive. In those circumstances, and given clear objection that the MNOs had against the use of the equipment, I held that it was unlikely that the fear of being found to commit an abuse would have constrained the conduct of the MNOs and forced them to supply SIM cards on demand. The unwillingness of the MNOs to provide SIM cards should have been taken into account in reducing the quantum of the loss alleged to have been suffered.

Claims for the loss of a chance

23. The analysis of attempting to predict the how third parties would have acted in the counterfactual world if matters had been different leads also to a different point. This is where the counterfactual involves deciding whether the claimant undertaking has suffered loss because it was prevented by the anti-competitive conduct from taking part in a tender or winning a contract.

24. This problem is not unique to antitrust counterfactuals but arises in various other contexts as well. The most usual one is where a claimant sues their lawyer or other professional adviser, for example for failing to lodge proceedings before the expiry of the limitation period. Whether the claimant has in fact suffered any loss depends on the court's assessment of how likely they would have been to succeed in the legal proceedings if the lawyer had not been negligent. If the case would have been hopeless anyway, then no loss has been suffered.

25. The English law on this is clear from a case called of *Allied Maples Group Ltd v Simmons & Simmons* [1995] 1 WLR 1602. The court takes the matter in two stages. First the court decides whether the claimant had a real rather than just a speculative chance of winning the tender or the contract. If they did not have a real chance then the inquiry ends there. If they did have a real chance then the court must consider secondly whether it was the abusive conduct of the defendant that prevented the claimant from being able to pursue the opportunity. If it was, then the court computes the profit the claimant would have earned if they had in fact won the contract or piece of litigation. Finally, the court applies a discount to that lost profit to reflect the fact that the claimant was not guaranteed to win to win the contract or tender.

26. Again, the *Albion* case provides a useful illustration. As well as the lost profit for the main contract with Shotton Paper, Albion argued that it had lost the chance of tendering to supply water to a neighbouring plant, a steel plant Corus Shotton which also required a large supply of water. There was evidence that the steel plant was unhappy with its current supplier and had in fact approached Albion asking them to tender. The Tribunal held on the basis of that evidence that Albion would have had a good chance of winning the contract. We also held that the reason Albion had been unable to follow up the inquiry made by Corus Shotton was that all its resources were devoted to fighting the abusive conduct of the defendant. We were able to calculate the profit that Albion would have earned on the Corus Shotton contract if they had won it. Finally, a discount of one third was applied to reflect the fact that Albion was not guaranteed to have won the contract.

27. The position arrived at in *Albion* can be contrasted with the situation in *Enron Coal* where the whole damages claim depended on the assertion that if a non-discriminatory price had been charged by the defendant, EWS, then Enron would have been able to submit a better tender for the long term contract to provide haulage services to Edison Mission Energy ('EME') and whether it had a good chance of winning that contract.

28. Interestingly the parties approached the question of how to prove this point in very different ways. The Claimant produced an expert witness, an economist with a well known litigation consultancy firm who gave evidence about whether the third party, as a rational economic decision-maker would have preferred the claimant's bid and so given them the contract. The Defendant's main defence was that the question for the Tribunal was not whether a hypothetical, rational decision maker would have accepted the Claimant's bid but whether the actual third party, EME, would have accepted it. On this point they were able to provide evidence from a witness, Mr Crosland, who had actually been in charge of the decision within the third party EME at the time as to which bid to accept. His evidence was that for various reasons they would still have rejected Enron's bid even if there had not been the price disadvantage.

29. The Tribunal first had to deal with the question which approach was right – should the court base the 'but for' world on how an economically rational decision maker would have behaved, and rely on expert evidence about that or should it base the decision on how this particular third party would have behaved, if there is evidence available about that?

30. The Tribunal held that the question was how EME would have behaved. It accepted that there may be a problem that the witness' evidence may be coloured by what *in fact* happened when he comes to say what would have happened in the but for world. Therefore the Tribunal should look at the context in which the negotiations were taking place, at contemporary documents, and in some important respects by other witnesses. The Tribunal found that the reasons the witness gave in his evidence at trial for why he would have rejected the Enron bid were supported by a contemporaneous email that he had sent at the time to his colleagues. Both showed that price was not the only issue. Flexibility in the service to be provided and a good working relationship were also important.

31. The point about a good commercial relationship turned out to be significant. Enron and EME had previously worked together on a project and that had turned sour before the abuse had been committed. There was no reason to expunge this acrimonious history from the counterfactual world. The Tribunal said of the EME witness' evidence:

> "Mr. Crosland stated strongly that there was a "general presumption" that EME would have preferred not to deal with ECSL owing to their past relationship and that having "been bitten once and we were careful not to be bitten twice." We accept this as a significant statement."

32. There were many other factors that the Tribunal considered as well in coming to its conclusion that Enron did not have a real chance of winning the contract even in the counterfactual world where the abuse had not taken place. The Tribunal's conclusion that it really had no such chance meant that the claim for damages failed.

33. The availability of witnesses can thus be crucial to constructing the counterfactual even if their view is inevitably coloured by what has in fact happened. In *Enron* there was an

additional issue, namely whether the claimant would actually have bid for the work at all as well as the issue whether Mr Crosland would have chosen them if they had bid. Because the claimant Enron was in liquidation by the time it brought the case, the Defendant was able to call as a former employee who have evidence that the claimant had not been serious about bidding for the work. A similar situation arose in *2 Travel* where the defendant was able to call as a witness in its defence a former finance director of the Claimant to say how poor the financial situation of the Claimant had been, even before it was affected by the infringing conduct.

Alternatives to counterfactuals

34. The title of this conference invites us to consider what are the pros and cons of counterfactuals. Any examination of the 'cons' begs the question: what is the alternative? One alternative that is discussed in to legislate for assumptions as to what would have happened in the absence of the abusive. For example, should a court simply assume that in the absence of a price fixing cartel the price paid by the cartel members' customers would have been 10 or 20 per cent lower than the price they paid? For example, in the Hungarian Competition Act, an amendment that came into force in June 2009 provided that in a claim for damages resulting from a supply-side price cartel, there is a presumption that the prices charged were increased by 10 per cent.

35. The United Kingdom Government consulted on whether there should be a rebuttable presumption of loss in cartel cases and if so what should the figure be. In its publication of the outcome of the consultation in January 2013,[5] the Department for Business, Innovation and Skills recorded that the majority of people who had responded on this question were opposed to any such presumption. Some respondents considered that it would shift the scales of justice too much in favour of the claimant whilst others observed that it would be a departure from the normal English law position that loss must be proven. Other respondents argued that it was unlikely to save time, as in most circumstances both claimant and defendant would seek to rebut the presumed loss by adducing evidence. It was also pointed out that the distribution of cartel overcharges is very wide, with some cartels causing no overcharge at all, so that to presume any specific number would be inappropriate.

36. In my view, presumptions as to a particular quantum of loss are not a substitute for a properly devised counterfactual. In any event, heads of loss can extend beyond simple loss of profit, for example, the loss of a chance claims in *Enron Coal* and *Albion*. In *2 Travel* there was a claim for the loss of the asset value of the business which had gone into liquidation, it was alleged, as a result of the predatory abuse committed by the Defendant.

[5] Ref: BIS/13/501 Published: 29 January 2013

37. Finally, there is the Commission's proposal for a Directive on certain rules governing actions for damages under national law for infringements of the competition rules,[6] the Commission's Staff Working Paper and Practical Guide to quantifying harm in damages actions.[7]

38. Article 16 of the proposed Directive requires Member States to legislate so that in the case of cartel infringements there is a rebuttable presumption that the cartel caused harm. Article 16 further provides that the burden and standard of proof must not render the exercise of the rights to damages impossible or excessively difficult.

39. More interesting, perhaps, is that it also provides that Member States must provide that the court 'be granted the power to estimate the amount of harm'. I am sure that this would be a useful pointer. In the *Recall Support Services* case, much of the evidence and argument related to quantum and the counterfactual. The counterfactual was particularly difficult to devise in that case because the restriction had, it was alleged, choked off the use of the telecoms apparatus just as the Claimants' businesses were starting to develop. The Claimants had no track record on which it was possible to base projections as to how the business would have developed and hence how much business had been lost. The Defendant's expert drew attention to all the uncertainties arising in trying to construct the counterfactual and the Defendant submitted that because of that, it was impossible to arrive at any meaningful quantification of loss. The court should therefore just award nominal damages. As I held that the *Francovich* criteria were not satisfied, quantum did not actually arise for decision. But I said that if it had, I would not have heeded the Defendant's counsel of despair but would have attempted to devise a counterfactual as best as I could. That must be the right approach. Damages would only have needed to be computed in that case if there had been a sufficiently serious breach of EU law to sound in damages. Similarly in a competition infringement case, there is, *ex hypothesi*, a breach of law that has caused loss. The courts should do their best to arrive at some proper computation of that loss even if it is necessarily an estimate.

40. The Commission's Staff Working Paper and Practical Guide are firmly founded on the basis that defining a counterfactual is what the court has to do. Much of the Guide relates to quantifying damages in actions against cartel members. Our experience in the English courts is that this has not been the area where cases have in fact arisen for decision. There are certainly many claims brought against cartel participants but they have so far generated many initial procedural disputes or have settled before the court has had to tackle these difficult issues.

41. There is a section of the Guide which deals with damages claims for exclusionary abuses, both where the claim is brought by an existing competitors who loses business as a result of the abuse and by a would be market entrant who cannot get his business started because of the exclusionary conduct. It must be said that not much of what the Guide

[6] COM(2013)404 final published 11 June 2013 and available on the Competition Directorate's website. See also the Communication from the Commission at Official Journal 13.6.2013 vol C167 p. 19.
[7] SWD(2013) 205 (11 June 2013)

says would have been of great help in the cases described in this Paper. Perhaps this proves that these claims all depend on their own facts.

42. One point that is relevant to how national courts approach counterfactuals is that competition law is not the only area of law where this task has to be undertaken. I have already referred to the case of the negligent valuer that was relied on by the Tribunal in *Albion*. Leading cases on counterfactuals in the English courts include a case where the owner of a Greek restaurant claimed damages for loss of a profitable business as a result of his landlord's failure to keep the premises in good repair[8] and the likely financial instruments trading that the victim of a fraud would have engaged in if he had not been deprived of his funds.[9] The courts feel confident in making these assessments, as best they can.

43. When someone tries to predict the future, they can be sure that as time passes they will be shown either to have been right in their predictions or to have been wrong. One advantage of counterfactuals is that, when predicting the past, it is impossible to say whether the court is right or wrong in the conclusions it reaches.

[8] *Vasiliou v Hajigeorgiou* [2010] EWCA Civ 1475
[9] *Parabola Investments Ltd v Browallia Cal Ltd* [2010] EWCA Civ 486