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Competition law: Rising up the agenda

Suzanne Rab and Alex Olive of Hogan Lovells examine the OFT's new approach to disqualifying directors who 'ought to have known'



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COMPETITION LAW: RISING UP THE AGENDA

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1 Introduction

In 2003, the UK's competition regulator, the Office of Fair Trading ("OFT") was given the power to seek a competition disqualification order ("CDO") allowing for disqualification of a director if a company has breached competition law. On 29 June 2010, the OFT published new guidance on the use of CDOs (the "Guidance"), potentially signalling a more aggressive enforcement stance. The new Guidance includes a number of policy changes designed to strengthen deterrence of competition law breaches, alter boardroom dynamics and encourage a top-down compliance culture.

This article reviews the OFT's new policy and its likely impact in practice. (References to the OFT in the context of applying for a CDO also apply to a UK regulator with concurrent competition law powers.)

2 What is a competition disqualification order?

The Company Directors Disqualification Act 1986 ("CDDA") sets out circumstances in which the court may or must disqualify an individual from acting as a director of a company. For these purposes, a director is any person who acts as a director of a company, whatever their title. This includes a *de facto* director and a shadow director.

In a competition law context, the power arises where a company is found to have breached either:

- the prohibition against anticompetitive agreements (under Chapter I of the Competition Act 1998 ("CA98") or Article 101(1) of the Treaty on the Functioning of the European Union ("TFEU")); or
- the prohibition against abuse of a dominant position (under Chapter II of the CA98 or Article 102 TFEU).

Under the CDDA, the court must make a CDO against a person if the court considers that the following two conditions are satisfied in relation to that person:

- an undertaking which is a company of which that person is a director commits a breach of competition law; and
- the court considers that person's conduct as a director makes him or her unfit to be concerned in the management of a company.

During the period of a CDO (up to 15 years), it is an offence for the individual to act as a director of a company or a receiver of a company's property, be concerned in a company's management or act as an insolvency practitioner.

A CDO may be sought from the court by the OFT or by a regulator with concurrent powers. The OFT is also able to seek competition disqualification undertakings ("CDU") from directors in place of applying for a CDO. A CDU has the same effects as a CDO, but the term accepted by the OFT might be less than under a CDO.

Criminal sanctions for individuals in respect of competition law infringements are not uncommon in other jurisdictions, within the EU and beyond, and such sanctions can also involve a ban on acting as a director. However, the UK's standalone director disqualifications are relatively unique.

2.1 OFT consultation and impetus for change

On 18 August 2009, the OFT issued a consultation on its proposed changes to its 2003 guidance on CDOs, seeking to maximise their deterrent effect.

The OFT consulted on the deterrent value of CDOs for individuals, in contrast to the deterrent effect of sanctions

against the company alone. While most respondents agreed with the OFT that CDOs have a deterrent value, some warned that greater use would have a disproportionate effect on small companies. In response, the OFT considers that individual deterrence is important and that this in turn protects the public. The OFT also commented that CDOs ought to apply to companies of all sizes.

The Guidance is significant for two key reasons. First, it gives a warning shot to directors that it will increasingly consider using these powers. This implicitly recognises that, to date, it has not been actively used as an enforcement tool. Second, perhaps more meaningfully, it targets complacent or cynical behaviour of directors who – for example – fail to ask questions about their business practices.

Directors are clearly considered by the OFT as being responsible – in a truer sense – for their department or team. One of the key issues raised by the OFT’s consultation was a proposal for the OFT to retain a discretion to apply for a CDO in all cases where it thinks that a director is unfit to be concerned with the management of a company. Under this approach, the OFT would no longer limit the use of CDOs to cases where the director was directly involved in or contributed to the breach. Instead, the OFT would also be likely to apply for a CDO where a director knew about a breach and failed to take steps to prevent it, or where a director *ought to have known* about a breach. Further, the OFT establishes a core standard of competition law knowledge, asserting that “every director of every company ought to know that price-fixing, market-sharing and bid-rigging are likely to breach competition law.”

3 The OFT’S approach to director disqualification

The Guidance sets out the following five-step approach that the OFT will take to assess whether it is appropriate to seek a CDO.

3.1 Step 1 – breach of competition law

The OFT will first consider whether a breach of competition law has been proven in a decision or judgment by a UK regulator, the European Commission or a relevant, competent court.

The OFT may also apply for a CDO where there is no prior decision or judgment, provided it can satisfy the court that there has been an infringement of competition law. The OFT limits this to “exceptional” cases. However, it is nevertheless a contentious principle that directors may be targeted where the company itself has managed to avoid a finding of infringement. The OFT explains this may arise where the undertaking has been liquidated. Intriguingly, it also hints at the OFT’s ability to use the CDO process to fast-track a matter, by avoiding the full decision-making process under the CA98.

Where a competition law breach has been proved in a European Commission or European Court decision or judgment, the OFT intends only to apply for a CDO where the breach had an actual or potential impact on the UK. This also reveals the potential situation where an EU infringement decision does not extend to the UK, but the OFT nevertheless has sufficient evidence of infringement.

Any CDO application will not be made while an infringement decision remains subject to appeal.

3.2 Step 2 – nature of the breach

The Guidance provides that it is more likely to consider CDO applications where there has been a “serious breach.”

The imposition of a financial penalty (of any kind) is indicative of the breach being serious but the OFT having added the possibility of a serious breach failing to attract a fine. The OFT deflected strong criticism of this policy, arguing that it sends an important deterrence message. The policy is most likely to apply where a company has avoided paying a fine because it is small, or operates in a small market.

3.3 Step 3 – immunity and leniency

The OFT’s policy is that a CDO will not be applied for against any current director of a company if the company has benefited from leniency and the CDO relates to the conduct specifically benefiting from the grant of leniency. The OFT, therefore, encourages directors to ensure that their companies seek leniency in order to be “immune” from the possibility of a CDO. However, when doing so, directors will need to be careful that their conduct is squarely captured by the scope of the leniency application.

Moreover, the OFT may still consider applying for a CDO where:

- a director has been removed or otherwise ceases to act as a director of a company, owing to his or her:
 - (i) role in the competition law infringement; and/or
 - (ii) opposition to the relevant application for leniency; or
- a director fails to co-operate with the leniency process. By this the OFT is setting a high standard: the director must maintain continuous and complete continuation through the OFT’s investigation and until the conclusion of the matter.

By addressing the director’s role in the leniency process and their continued connection with the company, the OFT is seeking to better align the often opposing incentives of directors and

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companies when under investigation. Directors must take separate legal advice when involved in an infringement case to ensure they adequately distinguish an infringement from the reason for leaving a company, especially if the company takes disciplinary action, seeks to “negotiate” a resignation, and/or dismisses the director concerned.

Although the OFT insists this policy does not undermine the leniency regime, it undoubtedly presents an additional factor to be considered by the very individuals considering leniency applications.

3.4 Step 4 – extent of the director’s responsibility for the breach

Perhaps the greatest step-change in the Guidance is the consideration of a director’s responsibility for a breach.

In all cases the OFT will consider whether:

- the director’s conduct contributed to the breach of competition law;
- the director’s conduct did not contribute to the breach of competition law, but he had reasonable grounds to suspect that the undertaking’s conduct constituted the breach and took no steps to prevent it; or
- the director did not know but ought to have known that the undertaking’s conduct constituted the breach.

The OFT’s guidance in respect of a director’s conduct having contributed to the breach is relatively straightforward, and is not new. The OFT will consider any evidence of the director, either alone or with other persons, having:

- actively taken steps to carry out the infringement;
- planned, devised, approved or encouraged the activity which caused the breach; or
- ordered, pressured or encouraged others to engage in the activity causing the breach.

Evidence that a director had reasonable grounds to suspect that the undertaking’s conduct constituted the breach may include the director’s knowledge about colleagues’ conduct and/or of the use of funds to finance activities relating to the breach. The concept of “reasonable grounds to suspect” is untested in this context.

When considering whether a director did not know but ought to have known that the company was involved in the breach, the OFT is likely to consider, among other things, the following factors:

- the director’s role in the company, including his specific position and responsibilities;
- the relationship of the director’s role to those responsible for the breach;
- the general knowledge, skill and experience actually possessed by the director in question and that which should have been possessed by a person in his or her position; and/or
- the information relating to the breach which was available to the director.

Directors are not expected to have specific expertise in competition law. However, they are expected to appreciate the importance of competition law compliance and to know that price-fixing, market-sharing and bid-rigging agreements are likely to breach competition law.

This has important ramifications for directors’ own career-management, spelling out the need to have a firm grasp of competition law compliance and how to apply compliance principles to the day-to-day work of the company. This will most likely affect senior directors of large companies, who would previously have been saved by the absence of actual, hands-on involvement in or knowledge of the conduct in question.

3.5 Step 5 – aggravating and mitigating factors

Having considered the issues listed above, the OFT will then consider whether there are aggravating or mitigating factors in relation to a particular director. These are unchanged under the new Guidance.

Aggravating factors include evidence that the director:

- had been directly or indirectly involved in breaches of competition law in the past;
- dishonestly destroyed or advised others to destroy any records;
- obstructed or impeded any investigation by the OFT, a UK regulator or the European Commission (or attempted to do so or advised others to);
- during an investigation, unlawfully refused or advised refusing access to investigators to the undertaking’s premises;
- ordered, encouraged or advocated continued participation in the breach following an investigation.

Mitigating factors include evidence indicating:

- coercion by another undertaking (e.g. to avoid threatened retaliation by a dominant undertaking);
- genuine uncertainty prior to the breach as to whether the infringing activity constituted a breach;
- the director contributed to the company taking quick remedial steps when the breach was brought to his or her attention;
- the director took disciplinary action against the employees responsible; or
- the director was under severe internal pressure (such as from controlling shareholders of the company or directors of a parent company) either to be involved in the breach or to allow it to occur (although pressure to meet sales or profitability targets will not be mitigating factors for this purpose).

4 Implications in practice

Directors would be advised to take positive, ongoing steps to ensure that the aspects of the business under their watch do not breach competition law, including:

- familiarising themselves with the company's competition law compliance guidelines and requesting additional training if they are in doubt about any issues;
- understanding the activities of their company, its relationships with suppliers, customers and competitors, and the dynamics and competitive conditions of the markets in which the company operates, to enable them to identify particular areas of competition law risk and take appropriate action;
- seeking or recommending that the company seeks expert advice on the application of competition law to concrete situations;
- demanding that management uses more real-time information on which to base its commercial decisions. This may include information on the evolving market position of a company signalling a heightened antitrust risk;
- if breaches are detected, ensuring that remedial action is taken promptly and, if necessary, that appropriate disciplinary action is taken against relevant employees;

- monitoring the company's competition law compliance in the business areas within their specific responsibility.

More generally, the following principles and practical steps can help minimise the risk of falling foul of competition law and the associated risk of disqualification:

- seeking clear and ongoing sponsorship of a competition law compliance programme from the Board (and instituting one if this is not in place);
- integrating competition compliance with other areas of risk management such as bribery, corruption and securities regulation; and
- establishing clear mechanisms for reporting, monitoring and audit, ensuring risks are escalated and addressed quickly and effectively.

The fact that the company has such measures in place will not absolve an individual director from responsibility if he “ought to have known” about a breach and failed to take steps to prevent it. However, such steps will contribute to preventing such risks of non-compliance materialising or escalating.

The new policy is not without its difficulties, and the OFT will want to choose its cases carefully in the absence of any precedent

5 Conclusions

It may be that the heightened deterrence achieved by the Guidance alone is consistent with the OFT's mandate to promote a compliance culture. However, the credibility of CDOs will depend on their use. Clearly, disqualification of one or more high-profile individuals would provide the OFT with publicity needed to focus the minds of individuals on personal responsibility for competition law compliance. The new policy is not without its difficulties, and the OFT will want to choose its cases carefully in the absence of any direct precedent.

The OFT intends to provide further high-level guidance to directors on their responsibilities under competition law. It is hoped that such guidance will seek to ensure that the messages it sends will not excessively deter intelligent risk-taking and corporate investment that, in turn, drive the consumer benefits and efficiencies that competition law is designed to promote. ■

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