

At A Glance

## Quantification of Damage in the EU

### Overview

Competition law infringements such as cartels and abuses of dominant position cause economic harm to consumers and businesses. Victims of such infringements can seek compensation for damage suffered. Defendants, in addition to the fines imposed by the competition authorities, often face potentially enormous private damages claims. The efforts by the European Commission to bolster the private enforcement of competition law by encouraging more damages claims in Europe have contributed to an increase in such actions in European courts particularly in Germany, the UK, and the Netherlands. In addition, there are an unknown number of confidential disputes outside court involving often substantial claims.

### NERA's Experience

NERA has been involved in the quantification of damage supporting defendants and claimants in the US and the EU for many years. This includes extensive work on a wide range of international and national cartel damage cases, but is not restricted to cartel cases or competition cases only. In Europe in particular, NERA staff have worked on the quantification of damage in such contexts as the cartels in air cargo services, freight forwarding, cement, gas insulated switchgear, gas pipelines, liquid petroleum gas, rail tracks, roof tiles, sugar, coffee, automotive parts, chemicals, elevators and escalators, engineered wood products, as well as the manipulation of reference rates such as the LIBOR. NERA experts have taught European Commission-sponsored training seminars on quantification for judges in different jurisdictions, and have published on damage estimation in the context of US, European, and national law, as well as on the empirical tools underlying quantification. We have also been active in a wide range of international and national arbitration proceedings involving often substantial commercial disputes not relating to competition law violations.

NERA's breadth and depth of experience in the quantification of damages draws on the expertise from its many other practice areas, as well as on a worldwide network of renowned academics. NERA can thus provide unparalleled advice at the highest quality level and achieve the best outcomes for its clients.

### Introduction to Damages

Damage suffered and the compensation that can be claimed in a damages action always rely on a comparison of the actual situation the victim of a competition law violation finds itself in with the situation that the victim would have been in but for the infringement. This requires constructing a hypothetical counterfactual scenario corresponding to the profit or wealth situation that most likely would have emerged in order to contrast it with the actual situation. Thus, the construction of an appropriate counterfactual scenario is at the heart of every damage calculation even if not based on a competition law violation. The construction of such an appropriate counterfactual scenario also presents important conceptual and empirical challenges rendering the analysis methodologically demanding.

## Composition of Damage

Under EU law, it is generally accepted that compensation for harm suffered aims to place the injured party in the position in which it would have been had the competition infringement not occurred. As a result, the damage from a competition law infringement comprises three elements that have been recognized by the European Courts: the price effect (“*damnum emergens*”), the quantity effect (“*lucrum cessans*”), and the interest on the damages. For example, in the context of a cartel, the price effect is the actual loss due to the anticompetitive conduct defined as the reduction in margins of the purchaser due to higher (anticompetitive) input costs. That is, the part of the cartel-induced input price increase on the units that the purchaser continues to sell that is not passed-on to its own customers. The quantity effect is the indirect effect on the purchaser emerging from the profit loss due to a reduction in sales caused by the purchaser increasing its prices in response to higher input costs, that is, the margin that the purchaser would have made on the additional units that would have been sold in the absence of the cartel. The third element is an interest payment from the time the damage occurred until compensation is actually paid. Conceptually all three elements play an important role in damage calculation despite the fact that the price effect, often cast in terms of overcharge and pass-on, is the most prominent. The overcharge is the additional amount that a direct customer of the cartel needs to pay for the quantity it continues to buy. Pass-on denotes the part of the overcharge that is passed on in the value chain by the direct customer through the higher prices charged by the latter.

## Calculation Methods

In order to establish a counterfactual price or quantity, the most commonly used methods make use of comparator markets that are not affected by the anticompetitive conduct. A comparator market may either be the market for the affected product itself but before or after the anticompetitive conduct occurred (time-based comparator market), the same product in a different geographic region (geographic comparator market), or a different but structurally similar market (product comparator market). Using a so-called difference-in-differences analysis, the time-based comparator market concept may be combined with either of the other two comparator market concepts.

Each of these concepts typically requires the use of econometric methods such as multiple regression analysis to account for relevant differences between the market affected by the anticompetitive conduct and the respective comparator market used. For example, important input costs for the product in question likely vary over time as well as across geographic markets; they certainly vary across different products. Such differences in input costs need to be taken into account when estimating but-for prices on the basis of any comparator market. Thus, the valid and robust quantification of damages requires both a thorough understanding of the industry in question as well as expertise in the application of statistical methods to economic questions.

In addition to these comparator market-based approaches, other approaches to the quantification of damage have been proposed. One alternative approach involves the calculation of a but-for price for a product from the “bottom” up using information on production costs, including the cost of capital. Another approach to estimate damage is to compare the returns of a firm directly with its cost of capital: this approach assumes that in the absence of an antitrust violation, the claimant or defendant would earn their cost of capital, which reflects the returns required by investors to invest in that company. Both methods require, *inter alia*, expertise on calculating the cost of capital of an undertaking, e.g., using the concept of weighted average cost of capital (WACC), a standard measure of returns in regulated industries, or the capital asset pricing model (CAPM), which calculates the required return on a given asset by summing up the risk-free return and that asset’s risk premium.

Each of these methods entails different levels of complexity and is based on different underlying assumptions. As the method used to estimate the counterfactual scenario has the potential to substantially affect the magnitude of damage estimated and ultimately the compensation for damages, understanding the implications and the robustness of different methods and assumptions is of central importance.

## Practice Synergies

Advising defendants and claimants on damages claims requires a detailed conceptual knowledge of economics, finance, statistics, and econometrics. It also requires a thorough understanding of the market under scrutiny



and, potentially, the comparator market used. A specific advantage of NERA is that it systematically draws not only on its wide and deep experience in damage estimation itself but also on both the particular sector expertise stemming from regulatory work (e.g., in the energy or telecommunications sector) and the wider methodological expertise from other focus areas such as NERA's Securities and Finance Practice.

## About NERA

NERA Economic Consulting ([www.nera.com](http://www.nera.com)) is a global firm of experts dedicated to applying economic, finance, and quantitative principles to complex business and legal challenges. For over half a century, NERA's economists have been creating strategies, studies, reports, expert testimony, and policy recommendations for government authorities and the world's leading law firms and corporations. We bring academic rigor, objectivity, and real-world industry experience to bear on issues arising from competition, regulation, public policy, strategy, finance, and litigation.

NERA's clients value our ability to apply and communicate state-of-the-art approaches clearly and convincingly, our commitment to deliver unbiased findings, and our reputation for quality and independence. Our clients rely on the integrity and skills of our unparalleled team of economists and other experts backed by the resources and reliability of one of the world's largest economic consultancies. With its main office in New York City, NERA serves clients from more than 25 offices across North America, Europe, and Asia Pacific.

## Contacts

For more information or to contact our experts, please visit <https://www.nera.com/at-quantification>.