

Unclassified

DAF/COMP/LACF(2013)7

Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development

26-Jul-2013

English - Or. English

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

LATIN AMERICAN COMPETITION FORUM

Session III: Unannounced Inspections in Antitrust Investigations

Contribution from Chile (FNE)

3-4 September 2013, Lima, Peru

The attached document from Chile (FNE) is circulated to the Latin American Competition Forum FOR DISCUSSION under Session III at its forthcoming meeting to be held on 3-4 September 2013 in Peru.

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JT03343213

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LATIN AMERICAN COMPETITION FORUM

-- 3-4 September 2013, Lima (Peru) --

Session III: Unannounced Inspections in Antitrust Investigations

CONTRIBUTION FROM CHILE (FNE) *

1. Introduction

1. Historically, the Chilean National Economic Prosecutor's Office (*Fiscalía Nacional Económica* – FNE) experienced the challenge of investigating cases of anti-competitive agreements between competitors without the legal tools that have become the standard at a comparative level to ensure effective action against hard-core cartels: that is, an immunity and leniency system, the existence of severe penalties and – the reason for this roundtable – the possibility of surprise inspections or “dawn raids”.

2. Indeed, dawn raids – and, in the case of Chile, the interception of communications, as powers of investigation – were incorporated into Chilean law only in 2009, together with leniency. In parallel, with regard to the threat of severe penalties a significant increase in the statutory cap on fines took place first in 2003 and then in 2009.

3. Experience prior to 2009, i.e. prior to the incorporation of dawn raids and interception of communications (which, in practice, are often called “hard powers”) shows the enormous difficulties faced in order to satisfy the standard of evidence required to demonstrate an agreement between competitors from indirect and circumstantial evidence alone. This is in contexts where the authorities have great difficulty in accessing direct evidence. The Chilean cases known as Shipping Companies (2006), Oxygen (2006) and Isapres Private Health Insurance (2007) are perhaps a good illustration of this.¹

* A preliminary version of this contribution was prepared by Fernando Araya, lawyer and international coordinator, Mergers and Studies Division, FNE.

¹ In the first case mentioned above the TDLC convicted five shipping agencies for the simultaneous imposition of an additional charge for intermediation in export shipments. For the Oxygen case, the TDLC

4. While in later years, and even before the introduction of hard powers of investigation, the results of effective prosecution against cartels in Chile were noticeably better,² it was not until the introduction of effective investigation tools such as the interception of communications and dawn raids, together with a leniency system, that Chile has begun to gain the confidence that we have tools that are equivalent to those available to the competition authorities that have proven to be the most effective in pursuing cartels at a comparative level. However, these new tools impose significant challenges to implementation and years of experience of implementation by other competition authorities cannot easily be substituted by training activities, however intensive they may be.

5. In the remainder of this contribution we will set out in detail the legal framework on surprise inspection visits or dawn raids and broadly describe our experience in applying this new investigative power, without prejudice to the other laws and mechanisms that create an appropriate incentive system for effectively fighting cartels. In each case, we will refer to the main controversies that have arisen and how they were resolved.

convicted four medical oxygen suppliers for coordinated behaviour aimed at derailing a bidding process. In both cases, the convictions established by the court specialized in competition law were overturned by the Supreme Court. In both cases, the lack of sufficient evidence of collusive agreement was instrumental in the conviction being quashed. The rulings in these cases may be found here:

Shipping Agencies Case, TDLC: http://www.fne.gob.cl/wp-content/uploads/2011/05/sent_0038_20061.pdf

Shipping Agencies Case, Supreme Court: http://www.fne.gob.cl/wp-content/uploads/2011/03/csse_0038_2006.pdf

Oxygen Case, TDLC: http://www.fne.gob.cl/wp-content/uploads/2011/03/sent_0043_2006.pdf

Oxygen Case, Supreme Court: http://www.fne.gob.cl/wp-content/uploads/2011/03/csse_0043_2007.pdf

These criteria on a highly demanding standard of proof were collected at the split ruling of the TDLC on the *Isapres Case*, ruling out the existence of collusion due to the simultaneous and similar drop in prices in coverage of private health insurance plans by almost all operators in the system. However, the dissenting opinion in this ruling, as well as in the judgement of the Supreme Court – which was also divided – acknowledge the possibility that agreements between competitors can be proved by indirect evidence.

Isapres Case TDLC: http://www.fne.gob.cl/wp-content/uploads/2011/03/sent_0057_2007.pdf

Isapres Case, Supreme Court: http://www.fne.gob.cl/wp-content/uploads/2011/03/csse_0057_2008.pdf

² Omitting other significant cases, the development of case law is well illustrated if we take into account the decision by the Supreme Court in the *Plasma TV Case* (2008), in which for the first time the Supreme Court implicitly conceded that an agreement can be proven by circumstantial or indirect evidence (in the case, it was the pattern of increased calls between executives of competing companies and suppliers during a key period which decisively contributed to supporting the Supreme Court's ruling, but not the content of those calls, to which it never had access) and where in addition, for the first time, fines approaching USD 8 million were set and upheld. *Plasma TV Case*, Supreme Court: http://www.fne.gob.cl/wp-content/uploads/2011/03/csse_0063_2008.pdf

Subsequent to this development, in the *AmPatagonia case* (2008), an anticompetitive agreement among medical doctors in the city of Punta Arenas, for the first time the TDLC clearly distinguished the requirements to establish collusion between competitors, differentiating this offense from that of abuse of dominant position, something that the wording of the statute then in force did not help to clarify. *AmPatagonia Case*, TDLC: http://www.tdlc.cl/DocumentosMultiples/Sentencia_74_2008.pdf

Finally, the famous *Pharmacies case*, whose legal, media and political implications cannot be gone into here, but which remains, even to this day, the most emblematic case in the persecution of hard-core cartels in Chile. *Pharmacy Case*: <http://www.tdlc.cl/Portal.Base/Web/VerContenido.aspx?ID=3015&GUID=>

2. Legal framework in Chile to undertake surprise inspections visits

6. In its reasoning, the bill submitted by the President of the Republic in 2006 to make competition law more effective in prosecuting hard-core cartels, in connection with the raids, stated the following:

*“[T]he other main objective of the reform is to strengthen the powers of the National Economic Prosecutor’s Office, such that this service can adequately fulfil its duties as investigative body, particularly with regard to the detection and verification of collusive behaviour. / To the leniency system explained in the preceding paragraphs, the project adds as powers of the Prosecutor the opportunity to **request that the Police or Investigative Police undertake forced entry, search public or private premises and seize documents and records.** It also empowers it to request the same bodies intercept all kinds of communications. / These powers must be exercised only with prior approval of the Tribunal for the Defence of Free Competition, which in this area will act as a court to guarantee the rights of those under investigation. These new powers, together with the leniency programme, are a good complement to an efficient system in the investigation of collusive behaviour at the level of the most modern laws that exist in comparative law.”³*

7. The parliamentary process, which included extensive discussions on various subjects and a split decision on the constitutionality of some provisions of the bill that was finally approved,⁴ was accelerated due to an important event in the prosecution of cartels in Chile: the settlement between FASA and FNE. In April 2009, it was announced that the company Farmacias Ahumada (FASA), one of three pharmacy chains who had been accused by the FNE of collusion in late 2008, had reached a settlement with the FNE. Through this alternative outlet to the trial that was pending before the Tribunal for the Defence of Free Competition (TDLC), FASA acknowledged certain facts that made clear its participation in the collusive conduct in question, and agreed to cooperate with the FNE in the proceedings before the TDLC and agreed to pay an amount equivalent to USD 1 million in tax benefits.⁵ This event, which obviously caused a stir in public opinion, returned the bill that had remained pending since 2006 to the legislative agenda, and it was approved in July 2009.⁶

8. According to the wording of the provision adopted and its related legislation, the dawn raids carried out by FNE are subject to the following legal framework:

- The power to conduct dawn raids is described by law as follows: “Article 39. - [...] The powers and duties of the National Economic Prosecutor’s Office are: [...] n) In serious and qualified cases of investigation aimed at proving the conducts described in point a) of Article 3, to make a well-founded request and with the prior approval of the [TDLC], for authorization to the corresponding Minister of the Court of Appeals for the Police or Investigative Police, under the direction of an official of the [FNE] to indicate the application, to: n.1) Enter public or private premises and, if necessary, to force entry; n.2) Search and seize all objects and documents that may establish the existence of the offense; [...]”;

³ Presidential Message No. 134-354 of 5 June 2006 that set in motion the bill that eventually became Law No. 20.361/2009.

⁴ Constitutional Court Judgment, 23 June 2009, Rol 1377-2009.

⁵ Settlements can only take place once the proceedings before the Competition Tribunal have begun, and are proposed and must be approved by the TDLC. They have been regulated by competition law since 2003. However, the defence of other companies under investigation and part of the press, given the impact of the agreement with FASA, held that the procedure followed had consisted of leniency in circumstances whereby the law introduced by this latter mechanism was not yet in force.

⁶ Law 20361, DO 13.07.2009.

- This investigative tool can only be used in the case of the illegal actions set out in article 3a): this includes express or tacit agreements made between competitors, or practices established between them, which grant them market power and consist of fixing prices for sale, purchase or other trading conditions, limiting production, allocating market areas or shares, excluding competitors or influencing the outcome of tendering processes;
- The authorization for conducting searches can only be granted for *serious and qualified cases*: the case law of the TDLC and the Courts of Appeals, in response to the requests of the FNE to authorize the inquiries, which should specify what is meant by these;
- The possibility of conducting dawn raids is subject to a double preventive control: that the TDLC *approve* the request of the FNE for the exercise of hard power and that a Minister of the Court of Appeals of the place where the inquiries will be carried out, *authorizes* it. While the legislature has not specified the scope of preventive control exercised by either of the bodies mentioned, it is understood that approval by the TDLC requires certification that the information supplied by the FNE together with its request is reasonable evidence of an investigation into the illegal acts set out in article 3a) of DL 211, whereby the pursuit of the inquiries requested will be expedient and advantageous for the investigation; meanwhile, the authorization by the corresponding Minister of the Court of Appeals implies a verification that the inquiries will not infringe basic rights beyond what is strictly necessary to ensure the effectiveness of the measure;
- In dawn raids, searches and seizures, the FNE acts with the support of the Police and the Investigative Police;
- In these proceedings, the FNE is subject to a series of requirements and formalities that the Code of Criminal Procedure sets out for carrying out searches in criminal investigations. The rules by reference, in relation to dawn raids, concern: how to practice entering and searching locked premises, the schedule for the search, the contents of the search warrant, provisions the entering and searching special places, entering and searching places that enjoy diplomatic inviolability, the procedure for searching, monitoring measures prior to the court order, the implementation of entering and searching, the record of the proceedings, the seizure of objects and documents, retention and seizure of correspondence, the treatment provided to copies of communications or transmissions, the objects and documents that may not be seized and in relation to inventory and custody;
- For carrying out dawn raids, the Competition Law adds specific constraints: in particular, it states that the information obtained by the FNE as the result of a dawn raid may not be used for any other FNE investigation without obtaining a new judicial authorization;
- Compliance with the assumptions that authorize the raid and the requirements and formalities for its implementation is subject to an *ex post* check that may be brought by the party under investigation before the Minister of the Court of Appeals that approved the measure. When the performance or implementation of a raid has taken place outside of the provisions established by law or has not met the requirements laid out for it to proceed, the Minister will declare that the results of the raid (i.e., information and documents seized) not may be used as evidence in proceedings before the TDLC; even if the claim before the Minister of the Court of Appeals is unsuccessful, similar arguments aimed at excluding consideration of evidence, may additionally be asserted in the trial before the TDLC as a dilatory exception in response to the petition, challenging the documents when they are accompanied, in the comments to the proof and, in the event that the evidence obtained in violation of the law was considered by the Competition

Tribunal in its ruling, the matter may also be sent for consideration to the Supreme Court in the appeal against the ruling of the TDLC;

9. The ability to carry out dawn raids has certainly made it possible to overcome the limitations of evidentiary proceedings such as requests for information or inspection subject to the willingness of the companies under investigation, proceedings that always involve the filter of a counsel in terms of measuring out how much cooperation to provide in the case. Furthermore, insofar as they increase the probability of detecting and obtaining substantial evidence for conviction, raids reinforce leniency systems in force in the jurisdictions. In this sense, it is common practice that in sites where simultaneous inspections are practiced entrepreneurs and senior executives are informed about the possibility of participating in the leniency program.

10. However, from the viewpoint of the legal design, the mechanism could be improved. A major weakness is the lack of flexibility to modify entry and search permits. Unlike prosecutors who investigate criminal cases and who may ask the judge responsible for procedural safeguards to modify a entry and search permit over the telephone, in the event the FNE encounters significant changes in the inspection site to the circumstances that it took into consideration when planning its operation, the obstacles to change the judicial authorization are significant and, in any case, will remove the surprise factor, increasing the risk of destruction or loss of evidence. Another element of the system that has significantly increased litigation costs for the FNE is the different levels of complaint about alleged breaches of the formalities in the implementation of the entry and search measures. While it is essential that there is a complaint mechanism, the fact that the law does not provide for clear rules on the complaints process, deadline for filing, and persons authorized to make a complaint has proved an obstacle to completing the circle of the efficacy and legality of the measure. These problems, which involve an excessive expenditure of public and private resources in litigation, added to the suspensions of procedures that are usually ordered prior to resolution of these issues, could be avoided through a better synthesis of the process or a reduction of complaints mechanisms against the results of the raids, or a significant penalty when such challenges are shown to be baseless.

3. Experience of carrying out surprise inspection visits

11. The FNE has used the power to carry out raids sparingly, and has mainly reserved it for those cases in which the information gathered by the agency when deciding to submit requests for authorization indicates a high probability that, based on the facts, the procedure will be successful. Indeed, historically it has carried out raids no more than three times a year. The interception of communications has been authorized on a similar number of occasions.

12. To date, perhaps the best example of a raid is the one undertaken to gather evidence to prove an allegation made by the FNE currently in process before the TDLC, in the *Chicken Case*.⁷ The search in this case resulted in the obtaining of evidence that allowed the FNE to establish the participation of each actor in the operation of the collusive agreement, the modes of operation and the subjects on which it rested, in order to provide a basis for the case pursued by the TDLC.

13. The experience of the *Chicken Case* is also significant because the raid and the seizure of documents that took place generated a significant amount of litigation in different courts. In fact, the trade association to which the three major poultry companies belong and which was also accused by the FNE,

⁷ The allegation of the FNE is directed against three major poultry processors and the trade association they belong to. According to the FNE, there existed an agreement comprising several strategies to restrict production volumes. The requirement of the FNE can be viewed here: http://www.fne.gob.cl/wp-content/uploads/2011/12/requ_007_2011.pdf

has initiated two actions before the Court of Appeals of Santiago: a complaints procedure for violation of the requirements and formalities in the practice of the search procedure and an ad hoc demand for the return of documents seized. The complaints procedure was resolved in the lower court against the claimant and is awaiting the judgement on appeal. The request for return of documents, based on the infringement of the rights to defence of the applicant was resolved in favour of the latter on appeal. One of the accused poultry companies also filed an application for return of documents to the same effect to the Court of Appeals in San Miguel, but this was not accepted. Meanwhile, in the trial before the TDLC, some of the accused (principally the trade association) objected to the documents seized when these were added as evidence before the Competition Tribunal for alleged lack of integrity and authenticity, but the TDLC dismissed these objections.

14. Broadly speaking, the FNE protocols for the implementation of raids today consider the following stages:

- Careful advance planning: In the first stage only at the leaders of the operation. The rest of the team of the FNE and police or investigative police officers participating in the procedure become aware of it shortly before its implementation (the day before or the same day). In particular, the identity of the firm(s) and the location(s) to be searched is information that is revealed only at the time that each team approaches the premises to be searched, for the purpose of prevent information leakages;
- Pre-planning involves a painstaking description of the premises to visit with each team, the names and office locations and computers of senior executives, the location of the servers, etc. This information, which is usually extremely detailed, is not easy to obtain, but it is essential to ensure minimum effectiveness levels of the operation. The key is to minimize the uncertainty about the information to be located and not go hunting blind;
- During implementation of the operation a detailed record of all the proceedings and objects and documents that are seized will be completed. A chain of custody will be used and respected in relation to the objects and documents seized, to ensure that in the future evidence does not disappear and complaints about its handling are not raised;
- One of the main objectives will be to secure the computer server, so it is important that professionals with technical expertise in computer and information technologies take part in the operation;
- It is common at a comparative level that when a raid is carried out there already exists at least one applicant for leniency who has provided accurate information in order to proceed with the raid in question. Despite this, it is possible that the authority wants to encourage the cooperation of other companies subject to seizure, to which end it may be useful to inform them of the existence of a leniency program in the course of the operation;
- If the operation takes more than one day it will be necessary to isolate and seal the enclosure to prevent access to the owner, executives or other employees of the company. From the beginning to the end of the procedure, no company personnel may be allowed to remain alone and unattended by officials involved in the operation in those locations on the premises identified as sensitive from the point of view of the information that may be found there;
- Once the operation is complete, a record of all the proceedings, including a detailed list of the documentation that is seized, will be prepared;

- Following the operation and once in the offices of the competition authority, the stage of processing the information seized will begin, which may take several weeks or months. Generally this requires the support of experts in forensic work in information technology;
- On the part of those involved in the operation, it is always advisable to undertake an evaluation exercise on what went right, what went wrong and what can be improved for future raids.

15. While the FNE has some practical experience in the investigation of international cartels, to date it has not undertaken simultaneous raids coordinated with foreign competition authorities. So far, the FNE has not seen the need to ask any foreign authority to carry out an inspection in foreign territory for the purpose of gathering evidence. In the event that the FNE was formally requested by a foreign competition authority to carry out an inspection in Chile, it would have to comply with the beginning of an investigation and obtain the respective approval and authorization as described for it to proceed.

4. Preliminary assessment of the exercise of the power of carrying out dawn raids

16. The preparation for the implementation of these powers has involved intensive efforts to train professionals in the FNE. From 2009 to date, our professionals have received training from the U.S. Justice Department, the Canadian Competition Bureau, the National Competition Commission of Spain, and the competition authorities involved in the Cartel Working Group of the International Competition Network, among others. Additionally, we have worked closely in matters of training with prosecutors and the police forces in Chile. Without the assistance, exchange and guidance of our peers abroad and the entities responsible for the prosecution of crime in Chile, the FNE would not have been able to understand the enormous challenges implied by legal changes in the area of cartels, a unit that moved from working almost exclusively with an analytical approach to an approach of pursuing criminal behaviour (regardless of whether the system contemplates imprisonment for individuals or not).

17. However, no matter the number of training activities that are carried out, practical experience is irreplaceable. Each of the dawn raids and other operations carried out by the FNE so far provides invaluable lessons on how to improve future processes.

18. Moreover, it is important to note that the competition authorities may be faced by the industry lobby and business associations every time they carry out a raid, making it highly desirable to have a strategic definition regarding the use of this intrusive power, that anticipates all legal, political and media-related outcomes that its implementation might have.

19. The ideal scenario for the first raids undertaken by a competition authority will always be that the shortest time possible passes between their implementation and the filing of charges based on the evidence obtained thanks to the operation.

20. Finally, it should be noted that misuse of this important investigation tool can have unexpected consequences that, in the worst case, could cause the system of effective prosecution of hard-core cartels to lose its effectiveness. It is thus very important that competition authorities act strategically while making prudent use of this tool.