

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

Global Forum on Competition

INVESTIGATIVE POWER IN PRACTICE - Contribution from Brazil

- Session IV -

30 November 2018

This contribution is submitted by Brazil under Session IV of the Global Forum on Competition to be held on 29-30 November 2018.

More documentation related to this discussion can be found at: oe.cd/invpw.

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JT03439937

Investigative Powers in Practice

- Contribution from Brazil¹ -

1. Since the entry into force of Law 8.884/94, former Brazilian Competition Law, the competition authorities in Brazil have been allocating most of its resources to cartel repression. This effort comprehends the improvement of *ex officio* investigations, the conduction of joint investigations with criminal prosecutors (considering that cartel is also a criminal offense) and the strengthening of settlements programs. In 2000, the law was amended introducing the leniency program and authorizing the performance of dawn raids. The amendment set the foundations for the improvement of competition policy in the country. Nevertheless, a higher standard was really achieved in 2012 as a result of the enactment of law 12.529/2011. From this point, cartel enforcement became a top priority for the Administrative Council for Economic Defense - CADE.

2. The new law granted CADE with an appropriate structure, which resulted in the expansion and improvement of cartel enforcement and the allocation of more resources to investigations, leniency, and settlements. The way of managing cases was also restructured through the creation of specialized unities dealing only with cartel cases, such as the leniency, screening and intelligence unities. The new structure clearly separates the investigation phase from the prosecution phase (after the formal opening of the administrative proceedings for the defendants). In fact, this new way of internal management ensures that all the priorities (detection and prosecution) are addressed more efficiently and timely.

3. In addition, the new law has opened more room for the judgment of cartel cases at CADE's Administrative Tribunal, as a collateral benefit of the implementation of the pre-merger notification system. Since the implementation of an *ex ante* analysis, the General Superintendence (CADE's investigative body) is able to conclude most of the merger cases through the fast-track procedure. In that sense, the Tribunal analyses only the complex merger cases and has more time and resources to analyze anticompetitive conducts, most of them involving cartel cases. As a result, there is an increase in the number of cartel judgments and convictions over the years. It means that Brazil is now able to not only detect and prosecute cases but also punish the wrongdoers rigorously. This has been promoting awareness among the private sector, consequently raising deterrence and compliance.

4. Therefore, CADE has established a favorable environment for the development of cartel enforcement in Brazil. This is the result of a huge effort to develop a system towards the deterrence of cartels, after years having the cartel repression as a priority. Some of the efforts, which are the pillars of cartel enforcement in Brazil, will be highlighted below:

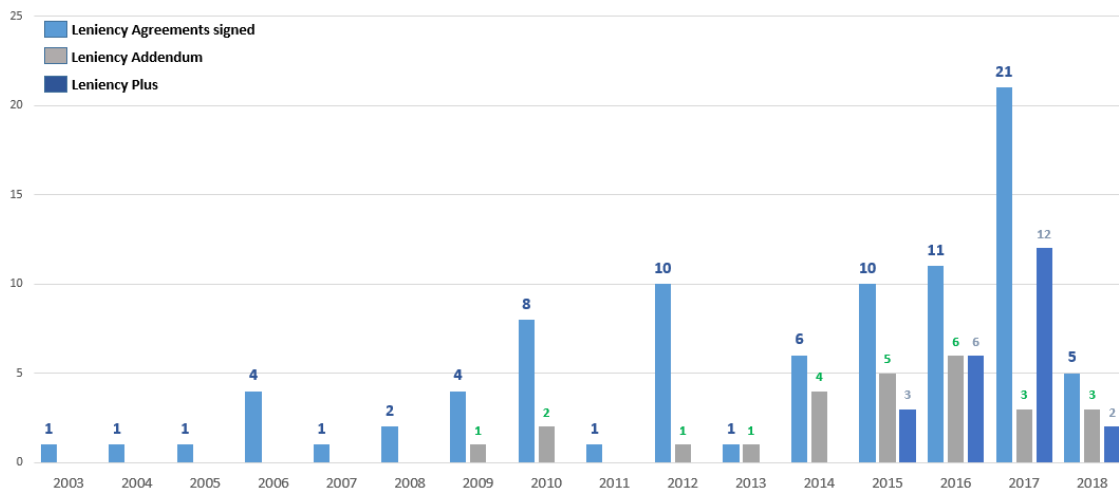
¹ This written contribution was prepared by Mr. Diogo Thomsom de Andrade, Deputy Superintendent of CADE, and Mr. Felipe Leitão Valadares Roquete, Head of the Intelligence Unit of CADE.

1. New and best practices in the leniency program

5. Analyzing the evolution of the number of cases in a temporal perspective, it is possible to visualize the credibility of the Leniency Program and identify some inflection points that created opportunities to innovate approaches and research strategies for CADE.

6. According to the table below, it is possible to observe in 2013 an abrupt drop in the number of leniency agreements signed. In the previous years, there was a significant number of agreements in a limited number of markets, especially in auto parts and technologies in obsolescence process. At that time, CADE decided to invest human and technological resources to identify and to develop proactive techniques for detecting infractions to the economic order, based in the perception of a potential reduction of investigations based in leniency agreements.

Figure 1. Leniency Agreements



7. Therefore, CADE developed some initiatives aiming to map projects and techniques, carried out by other competition authorities. It allowed the design of a benchmark that later resulted in the “Brain Project”.

2. Investment in investigation techniques and information technologies tools to improve ex officio investigations and intelligence: the “Brain Project”

8. In 2014, Cade started the development of data mining instruments and economic filters to support the staff involved in the investigations and case handlers.

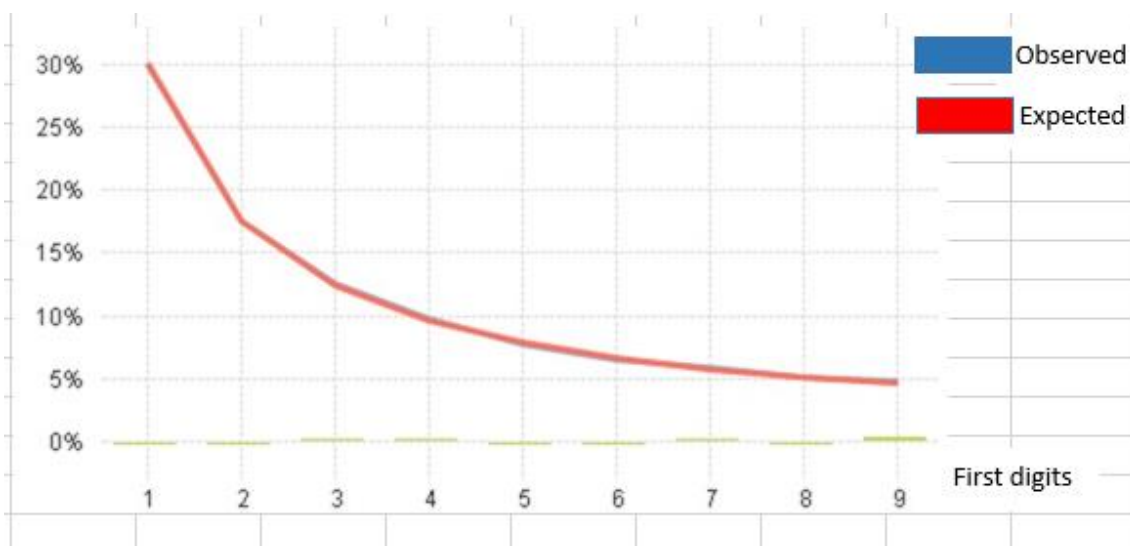
9. The data mining tools allow for the automatization of analyses formerly conducted by hand. The tools comprehend a set of techniques aiming at identifying evidence of bid rigging – such as suspicious, implausible facts or behavioural patterns with signs of simulated competition – and the provision of contextual information about the bids.

10. Regarding economic filters, based on specialized literature and econometrics, they seek to generalize evidence about the existence of cartels based on big data related to prices, costs, profit margins, market share and spatial econometrics. Through the identification of

companies' behaviour as described in academic articles, it was possible to derive mathematical models as statistical tests of general use in a kind of reverse engineering process.

11. For instance, one of the techniques under development aims to identify possible coverage proposals, according to models based on the Benford Law². The chart below shows the distribution of the first digits of the 6,401,859 closed proposals presented in federal bids from 2012 to 2016. The red line represents the expected distribution and the blue line represents the observed distribution. It indicates that the set of proposals follows the parameters of the mentioned Law.

Figure 2. First digits distribution: closed proposals



12. At the current stage of the project, it is possible to identify some questions that inevitably will be faced during the implementation of similar initiatives:

- Use of the results: the “battle” between intelligence (used only to prioritize markets and firms) and formal proceedings (used to start formal investigation);
- Data analysis: the difficulty to assess not only private markets data but also public procurement data of local governments, the difficulty to comprehend the data due to its quality and granularity, and the cost to get, transform and load the data.
- Human Resources: the difficulties linked to the recruitment and training of specialist staff in data science, which play an important role from database infrastructure up to computational science specialized algorithms;
- Translation: given the complexity of the techniques involved, the competition authority cannot ignore the costs related to the translation of the results to stakeholders (Judicial Branch, lawyers, firms etc.).

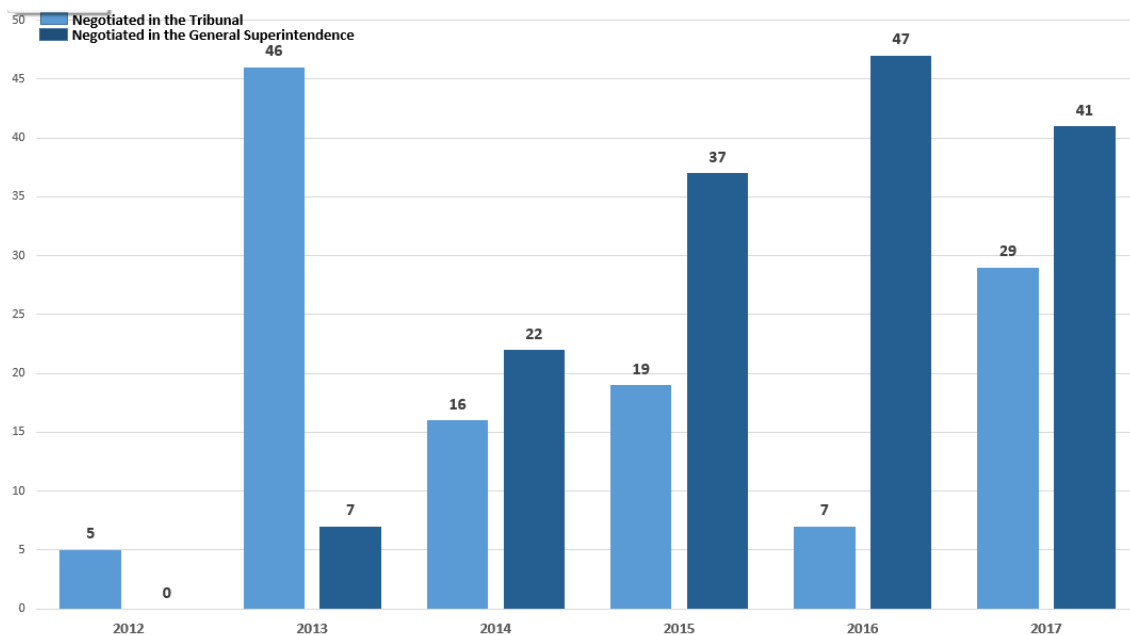
² This law describes how, in any given collection of numbers being studied, more of them will be likely to start with a 1 than any other number. 2's will appear at the beginning less often, 3's still less, and so on, at a predictable rate.

13. CADE’s experience gathered from the development of the “Brain Project” demonstrates that the use of proactive techniques to detect cartels is an additional element to the reactive tools. In other words, by means of the opening of an administrative proceeding that results in possible condemnations in the administrative sphere, the consolidation of economic filters certainly is an additional incentive for companies to sign, for instance, cease and desist agreements.

3. The development of a settlement system, aligning the incentives of both types of agreement (Leniency and TCC), in parallel to the implementation of new investigation techniques

14. The increase in the number of Cease and Desist Agreements signed shows that it is possible to defend the existence of a virtuous cycle resulted from the combination of the various investigative strategies. By this process, reactive (and consolidated) initiatives enhance the use of proactive (and innovative) initiatives, allowing a mutual reinforcement of the dissuasive effects along with the economic agents.

Figure 3. Requirement of cease and desist agreements homologated



15. Likewise, the framework involving the standardizing of the agreements negotiated by CADE, as well as the other strategies of investigation have its effectiveness amplified, bearing in mind, the construction of a partnership network with the bodies responsible for criminal prosecution.

4. Domestic Cooperation and Dawn raids

16. CADE sought to develop partnerships with other Brazilian public authorities, such as the Federal Court of Accounts (TCU), the Ministry of Transparency and Union Comptroller General (MTCGU), as well as the Federal Prosecution Service. These partnerships aim to enable the exchange of experiences in the development of innovative investigation techniques – such as the use of open data and big data, etc – and allow the planning and the conduction of joint investigations that may lead to dawn raids.

17. Therefore, it was possible to increase the effectiveness of the investigations. CADE can benefit from the inputs of the authorities responsible for criminal prosecution since they have exclusive powers to carry out invasive investigative measures, such as telephone interceptions, environmental tapping, etc. This allows the competition authority to deepen its investigations and, thus, to make search and seizure more efficient and focused.

18. Thus, Cade has developed initiatives to offer compensations to the agencies responsible for criminal prosecution, in order to expedite the post-search analysis. The main initiatives are to: (i) support the analysis of digital material (elaboration of a protocol analysis, selection of evidence in forensic software and generation of shared reports with criminal prosecution organs) and (ii) support the extraction of data from mobile devices (use of specialized equipment and development of analytical reports). Such initiatives have enabled the generation of timely results so that administrative and criminal investigations reach the expected results.

19. The success of this policy is shown in numbers³. In the last years the number of leniencies, settlements and leniency plus agreement have increased significantly. If we take these numbers alongside with the increase in the number of convictions of cartel cases and the amount of fines and pecuniary contributions paid for settlements, it seems clear that there is an increase in the deterrence of cartels in Brazil.

20. It is the “virtuous cycle” of the enforcement – the higher the risk of detection and conviction, the higher the awareness and the compliance. However, this cycle is dynamic. If the conditions of its maintenance in Brazil are established, new challenges are posed to CADE enforcement activity. Addressing these challenges is a key factor to continuous development. Indeed, alongside with its agreement policies – leniency and settlements – the last years have been marked by an investment in proactive investigations.

21. In that sense, it is symptomatic that half of the dawn raids ever carried by CADE have happened after 2012, although CADE already had the power to conduct search and seizure warrants since 2000. This policy of acting proactively is essential to keep the threat actual and, in that way, keep the incentives for leniency and settlements high.

22. Throughout the world, most of the authorities seem to have realized that they should not be over-reliant in leniency programs to raise deterrence. In Brazil, after the enactment of the new law, the competition authority has been able to establish a balance between cases initiated by leniency and cases proactively initiated by CADE. That feature of Brazil’s cartel enforcement has been one of the keys for its recent development. The challenge now is to develop new methods of *ex officio* investigations, including ones that take into account new frontiers of antitrust, like the increasing use of algorithms and machine learning and

³Cf. <http://www.cade.gov.br/servicos/imprensa/balancos-e-apresentacoes/apresentacao-balanco-2016.pdf/view>.

the use of virtual coins and virtual chains of custody in the economy, for instance. CADE has already begun to explore that frontier, by using algorithms to try to detect bid-rigging offenses and analyzing suspicious behaviors⁴.

23. Another challenge that the increase of importance of cartel enforcement brings to CADE is the relationship of this public enforcement with private enforcement and class actions. With more cartels convictions, the interest of private parties in sue the cartel wrongdoers has increased as well. The role of the authority regarding this developing field of antitrust and how to conciliate that with the incentives for leniency and settlements and with the public enforcement at all it's a challenge that should be addressed soon.

24. Furthermore, the success of CADE's enforcement regarding bid-rigging cartels and the recent surge of investigations that connects bid-rigging to other crimes, like bribery, corruption and money laundering, also presents a great challenge for CADE. The authority should work jointly with procurement authorities and criminal prosecutors in order to deter these complex cases and align the incentives among the variety of collaboration and leniency programs to ensure a coordinated enforcement. Actually, the biggest corruption investigation ongoing in Brazil, called "Carwash Operation", also contains cartel offenses.

25. Last, but not least, for an effective deterrence of cartels the enforcement should be (or at least try to be) as dynamic as the dynamism of the cartelists endeavors in the economy. In that sense and after seven years of the Law 12.529/11, there are rising debates regarding the adequacy of the fines imposed by CADE and whether the method of calculation of these fines and sanctions should consider aspects like the real damages in economy or the effective undue advantages obtained by the cartelists and how it should be considered. Regardless of the final understanding of CADE's Tribunal, as these discussions may directly affect several aspects of the investigations and enforcement, it's important that any definition on these issues take into account the need to preserve the milestones and achievements of CADE in fighting cartels in Brazil so far.

⁴ Cf., *exempli gratia*, <http://globalcompetitionreview.com/article/1143369/brazil-investigates-medical-equipment-cartels>.