

## Insights

# WHEN CAN YOU ARGUE MITIGATION? CAT REJECTS SUPPLIER MITIGATION DEFENCE AND ISSUES GUIDANCE FOR SCOPE OF SUPPLIER MITIGATION

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## SUMMARY

A Competition Appeal Tribunal (CAT) judgment recently obtained by BCLP on behalf of clients Royal Mail and BT has wide-ranging implications, not only for all competition follow-on damages claims but also many other forms of commercial damages claims. It sets out important guidance on the circumstances in which a defendant can plead that a claimant has mitigated its losses through negotiating lower costs with its suppliers, and thus that any liability of the defendant should be reduced accordingly.

Royal Mail Group Limited; BT Group Limited and Others v DAF Trucks Limited & Others is the first judgment interpreting the scope of the supplier mitigation defence articulated by the Supreme Court in Sainsbury's v MasterCard. Our clients succeeded in their argument that DAF's proposed amendments to its defence of mitigation through negotiation with suppliers had no prospect of success.

## BACKGROUND

Royal Mail and BT have issued proceedings against DAF alleging that they have been overcharged for the purchases of trucks as a result of the cartel in the trucks sector uncovered by the European Commission. The defendants deny that the cartel caused any such loss and are arguing in the alternative that any loss suffered will have been passed on to Royal Mail and BT's respective customers.

In its seminal judgment in Sainsbury's v MasterCard and Sainsbury's v Visa last summer, the Supreme Court explained how the law of "pass on" applies within the law on general mitigation of losses. It stated that when faced with an imposition of a cost, a merchant can respond in four main ways: (i) it can do nothing in response to the increased cost and thereby suffer a corresponding reduction of profits or an enhanced loss; (ii) it can respond by reducing discretionary expenditure on its business such as by reducing its marketing and advertising budget or restricting its capital

expenditure; (iii) it can seek to reduce its costs by negotiation with its many suppliers; or (iv) it can pass on the costs by increasing the prices which it charges its customers. The Supreme Court found that no legal mitigation would occur if solely options (i) and/or (ii) were pursued but that if option (iii) (“Supplier Mitigation”) and/or option (iv) (“Pass On”) were adopted to any extent, “the compensatory principle mandates the court to take account of their effect and there will be a question of mitigation of loss”.

The Supreme Court explained that whilst the legal burden lies on the defendants to establish mitigation, “once the defendants have raised the issue of mitigation, in the form of pass-on, there is a heavy evidential burden on the [claimants] to provide evidence as to how they have dealt with the recovery of their costs in their business.” Most of the relevant information will be exclusively in the hands of the claimant. The claimant must therefore produce that evidence in order to forestall adverse inferences against it.

Following the Supreme Court’s judgment, DAF sought to amend its defence to plead a defence of Supplier Mitigation together with its existing Pass On defence.

## NO CARTE BLANCHE FOR SUPPLIER MITIGATION

DAF argued that the Supreme Court’s judgment made it legally permissible to plead that the “Claimant will have sought to mitigate any increase in its input costs by virtue of any such Overcharge by negotiating lower input costs and/or otherwise reducing its costs of supply”. DAF relied upon a general theory that a business faced with increased supply costs in one area will seek to compensate for that extra cost by reducing other costs, in order to preserve profitability. DAF argued that, beyond invoking that theory, until it sees (via disclosure from Royal Mail and BT) how those parties approached issues of cost control and budgeting, it is not in a position to plead how Royal Mail and BT mitigated loss arising from the overcharge. Nevertheless DAF contended that Royal Mail and BT “would have” done so. It argued that this approach was effectively sanctioned by the Supreme Court’s judgment in *Sainsbury’s v MasterCard* and *Sainsbury’s v Visa*.

Royal Mail and BT objected to this. They argued that DAF’s mitigation plea had no realistic prospect of success, for reasons including that:

- the claimants were unaware of the secret cartel so could not have consciously undertaken any Supplier Mitigation;
- DAF had put forward no factual evidence to support its plea; and
- general theory regarding businesses seeking to recover their costs cannot itself be a sufficient basis to allow this form of defence to be pleaded.

Royal Mail and BT argued that if the defendants were right in their interpretation of *Sainsbury’s v MasterCard*, then this would give carte blanche to any defendant in a competition damages claim or

even in a variety of other commercial litigation cases to simply plead Supplier Mitigation and then put the claimant to the task of disclosing vast amounts of documents in the hope that some factual basis could then be identified from that disclosure for it to rely upon at trial.

## THE CAT'S JUDGMENT: SOMETHING MORE THAN ECONOMIC OR BUSINESS THEORY IS REQUIRED

The Tribunal rejected DAF's position. It agreed with the claimants that DAF's Supplier Mitigation pleading was not sufficiently arguable and did not have realistic prospects of success. It held that if a defendant was able to plead Supplier Mitigation in such general terms, it would throw a significant evidential burden on to a claimant.

The CAT emphasised that "it is not only in follow-on claims under EU and UK competition law where this issue may arise but many commercial claims for damages by businesses, where what is alleged is that financial loss was caused by a breach of contract that left the claimant to continue to run its business with its cash balance or income adversely affected. Even with a relatively straightforward case of non-delivery of goods in breach of contract, for which the claimant obtained a replacement supply in the market at greater expense, the claim for the difference between the contract price and the market price could be met, on this basis, with an argument that the claimant mitigated its loss on that contract by reducing prices on other supply contracts."

The CAT also found that there would be a real risk of the infringement of the principle of effectiveness "unless there is some basis other than pure theory for believing that a defence of mitigation has some factual basis for it and so can properly be pleaded."

The CAT, therefore, explained that they "do not consider that the Supreme Court could have been intending to countenance or encourage such an approach to pleading a defence of mitigation." It decided that "it cannot be enough for a defendant to plead that a claimant's business input costs as a whole were not increased, or that as part of the claimant business's ordinary financial operations and budgetary control processes its overall expenses were balanced against sales so that profits were not reduced."

The CAT concluded that "for a defendant to be permitted to raise a plea of mitigation in this way in general terms, there must be something more than broad economic or business theory to support a reasonable inference that the claimant would in the particular case have sought to mitigate its loss and that the steps taken by it were triggered by, or at least causally connected to, the overcharge in the direct manner required by the British Westinghouse principle."

## WHAT DOES THIS MEAN FOR OTHER CASES?

The CAT explained that what is sufficient to give rise to a defence of Supplier Mitigation will vary from case to case. Examples might include a claimant's knowledge of the nature and amount of the overcharge (such that it is inherently likely that a claimant would seek to address it); the relative

ease with which the claimant's business could be expected to reduce certain input costs or input costs generally; or the fact that other supplies made by the defendant to the claimant have been renegotiated in years following the increase in the prices alleged to have been caused by the anti-competitive conduct.

The CAT stated that it was not suggesting that a Defendant would need documents or evidence at the pleading stage to prove what the claimant did in response to the overcharge as it understood that such material is unlikely to be available to the Defendant prior to disclosure. Instead, what "is needed is some plausible factual foundation for the application of the broad economic theory in the way required to satisfy the British Westinghouse test that is relied upon, and for there being a causative connection between overcharge and cost cutting."

## **RELATED PRACTICE AREAS**

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## MEET THE TEAM



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