

Managerial Incentives and Leniency Policy *

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September 14, 2011

Abstract

This project investigates corporate directors and officers incentives to apply for leniency. The U.S. Leniency Act allows directors, officers, and employees to benefit from immunity of criminal prosecution if the directors, officers, or employees come forward to the antitrust agency. Evidently, this policy creates an incentive for workers' application, but relying on fairy morality tale as to a source of justification for such application seems highly implausible.

I propose a solution based on managerial incentive. The sole purpose of the board of directors (BOD) is to maximize the value of the firm. Once all potential tools of internal growth have been used and assuming that mergers and acquisitions are impossible to realize, a possibility of collusion emerge. To make it simple, I assume that directors simple care about collusion. So, to reach their objectives, they must create a collusion culture with their executives. I assume collusion can be implemented by a single executive: the chief executive officer (CEO).

In this static game, the BOD induces collusion via the CEO by creating a monetary incentive. The CEO remuneration includes a fraction of the firm to align both BOD and her/his objectives. The main contribution of this project lies in what follows. Due to its pivotal position and knowledge of the market, CEOs of all colluding firms receive (according to their ability) a signal about the likelihood that the antitrust agency opens an investigation for the cartelized industry. I consider a two firms industry. In this framework, a CEO applying for leniency keeps its position, and the firm stops its colluding activity by reverting to a more competitive arrangement.

Aubert et al.(2006) study the impact of the design of leniency policies on an effectiveness basis. They show that by including the employees as a potential beneficiary from leniency, collusion is deterred in a more effective way. Recently, Angelucci and Han (2011) find that shareholder coming forward for leniency should be granted only partial leniency, while individual employees should not be granted leniency. My study contributes to this scarce literature by assuming a different premise in assuming that shareholders are on the top of the pyramid.

The main result shows that when a high and low ability CEOs match, whenever the probability of the agency opening an investigation is sufficiently high, only the high ability CEO will apply for leniency and bring down the cartel. Consequently, with higher ability CEO, the leniency policy is beneficial for societal welfare.

The framework can be extended in several directions and much work remained to be done.

JEL classification codes: K21, K42, L41

Keywords: leniency programs, cartels agency problems

*The financial support of Fonds de Recherche sur la Société et la Culture (FQRSC) is gratefully acknowledged.

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