

STATE “INDIRECT PURCHASER” SUITS BENEFIT LAWYERS, NOT CONSUMERS

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Revisiting *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977) is a lesson from experience, with twenty-five years of litigation and legislation regarding the principle that, with limited exceptions, only those who directly purchase goods or services from businesses which violate antitrust laws (“direct purchasers”) can recover damages through private lawsuits.

Critics of *Illinois Brick* argue in good faith that the ultimate consumers’ (“indirect purchasers”) inability to recover damages somehow forgives antitrust violators from the full measure of payment for their errors, or at the least, compensates the wrong distribution plateau. *Illinois Brick* supporters, on the other hand, emphasize that antitrust law offenders must in fact pay three times, because damages are trebled, and should not have to pay again to successive tiers of claimants pursuing damage claims which are often quite speculative. History actually teaches that *Illinois Brick* supporters *should* include consumer groups, since the decision promotes antitrust law adherence, assured penalties, and resulting benefits for consumers, without imposing unfair penalties and unacceptable burdens on the judicial system.

Illinois Brick gestated from *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968). In that case, a customer (a shoe maker) sued a shoe machinery manufacturer under Clayton Act Section 4. The defendant argued that any over-charges were simply passed on to the ultimate shoe buyers. The Supreme Court said the shoe maker could recover its damages, since the indirect purchasers’ proofs of damages would be complex and speculative, and remote purchasers were less likely to sue.

This set the stage for *Illinois Brick*. The defendant made concrete blocks, which masonry contractors resold to general contractors as constructed sections. These general contractors used them to build and resell buildings to the State of Illinois and hundreds of counties, cities, housing authorities and school districts, all of whom sued the block makers for fixing the initial sales prices of the blocks.

The block makers cited *Hanover Shoe* for the proposition that *direct* purchasers could recover damages, even if they passed them on to the ultimate consumer. Using this rule, they argued that *indirect* purchasers could *not* recover because there could be duplicate damages for the same offense, and, essentially, sauce for the goose was sauce for the gander. The Supreme Court majority agreed: only *direct* purchasers can recover Federal antitrust damages, avoiding multiple liability, and sidestepping the uncertainties and difficulties in the ultimate consumers’ proof of damages.¹

¹This theme also is present in the “antitrust injury” quasi-standing requirement of *Brunswick v. Pueblo Bowl-o-Mat, Inc.*, 429 U.S. 477 (1977) and *Atlantic Richfield v. USA Petroleum Co.*, 495 U.S. 328 (1990) (an antitrust violation which increases competition may not result in “antitrust injury,”), and the specific standing principles of *Cargill v. Monfort of Colorado, Inc.*, 479 U.S. 104 (1986) and *Associated General Contractors v. Cal. St. Council of Constructors*, 459 U.S. 519 (1983) (Standing tests include directness of the causal connection, speculation prospects, potential for duplicative recovery or complex apportionment,

Well-meaning consumer advocates have objected to *Illinois Brick* ever since, making the simple, and facially appealing point (which the Supreme Court candidly made as well) that recovery would be denied to downstream indirect purchasers.²

One reaction to *Illinois Brick* was legislation in a minority of States³ and the District of Columbia permitting “indirect” consumer recoveries where antitrust claims are also brought under *State* competition statutes. However, these statutes do nothing to answer the underlying philosophy of *Illinois Brick*, or to solve the complex problems that the Court suggested. None of them, for example, require symmetry — that damages paid to upstream purchasers be deducted. *Illinois Brick* realized that the benefits to each member of a diffuse class are often so modest that compensation is simply ineffective, and therefore little is lost by limiting compensation to upstream tiers. The principal consumer beneficiaries are too often the plaintiffs’ lawyers, a problem acknowledged with regret by even vigorous consumer advocates.

Regardless of the obvious risks, these consumer advocates have recently intensified their call for a reconsideration of *Illinois Brick*. It seems plain, however, the same pragmatic balance should result, and that if changes are required, *Illinois Brick* should be extended to State cases or, at the least, consumer-level claims should credit upstream liabilities for the same offense. *Illinois Brick* and *Hanover Shoe* should go hand in hand, and if the ultimate purchaser recovers, then only a passing-on defense avoids multiple liability.

Limiting antitrust damages to the direct purchaser fully acquits the deterrence objective, more so than a series of consumer suits, since it more crisply defines the plaintiff group, and narrows the damages inquiry. The unwieldy alternative would be the judicial equivalent of an inverted value-added or excise tax assessment, permitting each tranche in the vertical distribution scheme to recover its segment of the over-payment, after the proof demanded by certainty and due process. Even the most conscientious jury would be daunted, and would likely resort to guesswork at best.

Critics of *Illinois Brick* reply that the ultimate consumers would just prove the amount of the illegal over-charge, and then treble it. The Supreme Court, however, concluded that the upstream purchaser might also have an independent reduced volumes claim, and the consumer would still have to trace the allegedly illicit price component downwards, a highly complicated judicial burden. Without *Illinois Brick*, the specter also exists of an expanding cascade of downstream plaintiffs, even beyond the classic consumer level. In order to assure fairness and foster judicial economy, presumably all of these constituent groups would have to be brought into the same proceeding, as their rights would be determined by the outcome.

There are economic theories galore for allocating over-charges among tiers of distribution, but they assume perfectly competitive markets, equal imposition of the over-charges, and a determined motive by the seller to maximize profits from discrete transactions. All of these elements may be entirely, partially, or not at all present in any specific case. In a best case scenario, the resolution would be left to conflicting testimony from several corners of experts. Markets are truly perfect only in classrooms.

In response to antitrust defendants’ complaints that they are faced with arguably unfair penalties for

and the existence of a more direct victim). A seriously divided Iowa Court recently acknowledged that its legislature had directed adherence to Federal principles, but nonetheless permitted an indirect suit. *Comes v. Microsoft Corp.*, (Iowa Sup. Ct. June 12, 2002).

²In 1999, food processors recovered \$1 billion from vitamin price-fixers, but there was “not a damn nickel for consumers – the ones who were truly hurt.” Howard Metzenbaum, President of the Consumer Federation of America, Statement Before the House Judiciary Committee on H.R. 4321 (Sept. 12, 2000), at 3.

³The status of State legislation is summarized in *Comes v. Microsoft Corp.*, (Iowa Sup. Ct. June 12, 2002).

their infractions, critics respond that “if you can’t do the time then don’t do the crime.”⁴ However, *Illinois Brick* concluded that the direct purchaser rule would actually *maximize* the likelihood of private lawsuit deterrents. The direct purchaser has the plainest damage case, with no risk of apportionment dilution and less complications than a tier group of plaintiffs. It is of course irrelevant to the defendants to whom damages are paid, so long as they are exacted.

Antitrust violations often are premised on exquisitely fact-intensive situations where the fact-finder can reach a fairly debatable conclusion. It is therefore important to business, competition, and the fair and efficient administration of justice that penalties are proportional to offenses, since disproportionate remedies could actually deter vigorous competition. The risk of unfairly draconian remedies is even more pronounced in the more amorphous antitrust categories, such as predatory pricing or Robinson Patman, where the fear of expensive litigation can have a chilling effect on otherwise energetic competitors. Consumers may lose if a price-reducing decision is not taken because of litigation risk, even where the abandoned action would have been entirely legal.

Yet, thanks to the aforementioned State laws rejecting *Illinois Brick*,⁵ indirect purchaser cases are now routinely thrown out of Federal court, but many State claims survive, based on exactly the same operative facts. These cases have inevitably resulted in complicated multi-state litigation with classes of remote consumers claiming violations far removed in the distribution chain.⁶ Defendants can simultaneously face the direct purchasers in Federal court and the indirect purchasers in State court, with the attendant removal, transfer, consolidation and other motions (which might not succeed), res judicata issues, discovery duplications, etc.

The results predicted in *Illinois Brick* have been fully realized. The indirect suits are extremely complicated, very time-consuming, burdensome to administer and defend, and fraught with the risk of multiple liability for singular antitrust errors.⁷ It is also certain that in most cases, the individual recovery will be modest to the point of not being worth its pursuit. The difficulty with most consumer class actions is not *Illinois Brick*; rather, it is that the individual class member’s damages are not only speculative at best, but usually not worth the effort to collect. In the typical class case, plaintiffs and defendants spend substantial time and resources to reach the class certification decision, and then settle, usually at an apparently arbitrary amount which (after legal fees) is often overwhelmed by administrative costs, with little of value to class members.⁸

Testimony conflicts and problems of proof generally also infect the indirect action. Economists will rarely agree on the accuracy or adequacy of the hypothetical damage model, and the intervention of middlemen brings inconsistency and inaccuracy into any damage calculation. While direct suits have similar impediments,

⁴In *Illinois Brick* the Justice Department argued that *Hanover Shoe* should continue to bar defendants from using passing-on as a shield, but that indirect purchasers should nevertheless recover treble damages for any overcharge. This position, the Court recognized, “ultimately fall[s] back on the argument that it is better for the defendant to pay sixfold or more damages than for an injured party to go uncompensated” and that “a little slop over on the shoulders of the wrongdoers . . . is acceptable.” The Court emphatically replied that “[w]e do not find this risk acceptable.”

⁵The Supreme Court has refused to invalidate these repeal statutes. *California v. Arc America Corp.*, 490 U.S. 93 (1989).

⁶Exactly the mischief anticipated by the majority in *Illinois Brick* has occurred with the multiple litigations alleging antitrust violations in the sale of everything from generic drugs to corn syrup.

⁷Even judicially-approved class settlements are not yet final in the sense that they can now be appealed by certain non-named plaintiffs. *Devlin v. Scardelletti* (U.S. S. Ct. June 10, 2002).

⁸In the vitamin cases, there were fines in the U.S. and the EU, settlements in direct purchaser and parens patriae cases, and ongoing state indirect purchaser cases. The Mylan and Microsoft cases have produced similar multi-jurisdictional proceedings for essentially the same alleged actions.

there are no intermediaries to complicate the process. The laws of supply and demand always apply, and economists are eager to explain how their client's prices were likely burdened by illicit elements, except if they were passed down to the next stage of distribution. In the typical "elastic" demand market, where the product is directly sensitive to price, more of the overcharges are absorbed at each tier than would be the case if the market is "inelastic" and therefore more of the overcharges are passed down. In addition, all of the other variables anticipated by Justice White in *Illinois Brick* usually come to roost, from differences in product size and grade, to OEM issues, to outside competition, and to entirely subjective pricing judgments. The problems multiply at each step as the increases become smaller (and harder to pass on without piercing a price point) and the consumers' interests wane to the point of indifference.

Thus, should *Illinois Brick* be reconsidered as consumer advocates insist? In fact it is reexamined every day in the State indirect purchaser cases, and Justice White's fears have come to pass, with an inappropriate balance in the form of any proportional payment to indirect purchasers. Deterrence of antitrust misconduct, compensation of the principal victims, and the furtherance of the antitrust goals of promoting competition and enhancing consumer welfare are all accomplished within the *Illinois Brick* umbrella. The unwanted effects, such as windfall recoveries for lawyers, modest to zero recoveries for consumers, procedural nightmares at massive cost for defendants — with unacceptable burdens on the judicial system — can all be traced directly to States' erroneous conclusions that consumer protection requires the right to sue in every case for every perceived wrong.

It has been estimated that two-thirds of the U.S. population has access to an indirect purchaser remedy under State law, despite *Illinois Brick*. To solve this, some suggest specific Federal preemption or mandatory consolidation of antitrust claims, combined in one forum, with all relevant constituencies represented.⁹ This possibility, which Justice Brennan suggested in passing in his *Illinois Brick* dissent, would involve intricate allocation debates and would no doubt be vigorously resisted by consumer advocates and the plaintiffs' bar.

In situations where consumers could benefit from the same certainty of recoveries as direct purchasers and the removal from the corporations of the unfair costs of multiple defenses and settlements, consumer groups might logically be vigorous *supporters* of an extension of *Illinois Brick* to State cases as well.¹⁰ Deterring companies from making energetic price decisions because of concern for marginal but expensive litigation frustrates the essential goals of the U.S. antitrust regime — protecting consumers and competition.

⁹See *In re Linerboard Antitrust Litigation*, pending in the Eastern District of Pennsylvania, and *In re Lorazepam and Clorazepate Antitrust Litigation* (D.C.Cir. May 14, 2002).

¹⁰Such a preemption would involve adjustments of *Illinois Brick* and *Hanover Shoe* as well, since the impetus for manufacturers would be the assurance that they would pay once, trebled if appropriate, and that penalty would fairly be allocated among the several tiers of distribution and eventual purchase which bore the burden of the illicit price. The savings in legal fees, and court requirements, and management time and effort, all would remain with the corporation for the benefit of its shareholders and for the benefit of future consumers.