INDIRECT PURCHASER LITIGATION:
ARC AMERICA’S CHICKENS COME HOME
TO ROOST ON THE ILLINOIS BRICK WALL

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I. INTRODUCTION: PERCEPTION VERSUS REALITY

The conventional wisdom within the antitrust community about indirect purchaser antitrust damages actions holds that:

- many, if not most, states have statutory or common law rules directing that their courts be guided by federal precedent in construing state antitrust law;

- some states have (but most have not) enacted “Illinois Brick repealer” legislation—which, under the Supreme Court’s decision in ARC America,¹ is not preempted by contrary federal rules;

- states without “Illinois Brick repealers” follow Illinois Brick² and, thus, do not permit indirect purchasers to sue for damages suffered as a result of price fixing or other Sherman Act violations;

- in the relatively few states that have enacted Illinois Brick repealers, thus allowing indirect purchaser actions, the rule of Hanover Shoe³ is expressly or impliedly overruled as well—so that, in an antitrust action by retailers against manufacturers, the defendants would not be liable for an overcharge that the retailers had passed on to consumers;

- because of the complexity of tracing overcharges through successive layers of distribution, even where state law theoretically permits indirect purchasers to sue for price fixing, such indirect purchaser litigation is of little economic significance; and finally,

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• while it may be rather odd that some states follow rules so different from those of Illinois Brick and Hanover Shoe, the anomaly is of little practical importance in the great scheme of things.

In truth, however, a growing number of antitrust plaintiffs are discovering what they perceive to be the possibilities inherent in state antitrust law and are calling the conventional wisdom into question. As a result, in a number of states—those “laboratories of federalism”—novel experiments are brewing.

As one would expect, state indirect purchaser class actions often follow in the wake of multidistrict federal direct purchaser class actions and/or a lawsuit or investigation by federal enforcers. Published sources indicate that there are pending state actions of this nature in the following industries subject to parallel Sherman Act proceedings in federal court: amino acid lysine, brand-name prescription drugs, citric acid, contact lenses, high-fructose corn syrup, and infant formula. Other recent state actions, apparently not parallel to pending federal actions, involve allegations in the aluminum and compact disc industries. In the latter case, a Tennessee trial court recently certified a class of all indirect purchasers at retail of compact discs in the states of Tennessee, Alabama, California, Florida, Kansas, Maine, Michigan, Minnesota, Mississippi, New Mexico, North Dakota, South Dakota, West Virginia, Wisconsin, and the District of Columbia—a grab bag of jurisdictions that either have Illinois Brick repealers or in which there exist other legal grounds to argue that indirect purchasers may sue.

Much more interesting than the sheer number of pending indirect purchaser cases, however, is the fact that plaintiffs have scored some


5 See infra notes 12, 25, 26, 27, 29 & 35.


7 Pertinent cases are cited infra note 35.


9 See infra notes 15, 18, 22, 23, 24, 25, & 35.


surprising preliminary victories in states without Illinois Brick repealer legislation. Notable are the following 1996 decisions from Arizona, Florida, North Carolina, Massachusetts, and Tennessee—all states whose legislatures have not acted to afford a remedy to indirect purchasers following the Supreme Court's decision in Illinois Brick.

In Arizona a trial court held recently that indirect purchasers have a claim for damages under state antitrust law,12 despite state statutory direction that the courts "may use as a guide interpretations given by the federal courts to comparable federal antitrust statutes,"13 and even though Arizona has a statute worded identically to the language of Clayton Act Section 4 as construed in Hanover Shoe and Illinois Brick. The court recognized that determining the amount of the passed-on overcharge would be a problem, but believed that the "clear statement of policy contained in the Arizona Constitution is to protect the citizens of Arizona from the precise conduct alleged by the Plaintiffs to have occurred here." An appeal is pending; the state attorney general supports the plaintiff's interpretation of Arizona law.14

In Florida an intermediate appellate court has certified to the Florida Supreme Court the question, "Does a consumer have standing to bring an action for damages under the Florida Deceptive Trade Practices Act ... for alleged price-fixing?"15 Plaintiff elected not to challenge on appeal the trial court's determination that Illinois Brick bars indirect purchasers from suing under the Florida "little Sherman Act," but reasoned that the operative provision of the state Deceptive Trade Practices Act16 forbids everything forbidden by Section 5 of the Federal Trade Commission Act,17 which in turn comprehends conspiracies in restraint of trade. The intermediate appellate court accepted this analysis, which proved persuasive because the court felt that in choosing between two bad alternatives—i.e., unusually complex litigation versus uncompensated consumer injury—compensation was more important than judicial efficiency.

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12 McLaughlin v. Abbott Labs., No. CV95-0628 (Super. Ct. Yavapai Co. Ariz. July 9, 1996), special action jurisdiction declined, No. 1 CA-SA 96-0215 (Ariz. Ct. App. 1996), app. docketed. (Many of the cases discussed herein name Abbott Laboratories, which makes both infant formula and brand-name prescription drugs—probably the most active of the pending state actions.)


In North Carolina the trial court dismissed a consumer infant formula class action on *Illinois Brick* grounds, but an appellate court has reversed.\(^{18}\) The court of appeals noted that the relevant statute\(^{19}\) was enacted in its present form in 1969, after *Hanover Shoe* but long before *Illinois Brick*. The court observed that during the years between *Hanover Shoe* and *Illinois Brick* a number of federal courts permitted indirect purchaser cases to proceed (see discussion below)—implying that if the *Illinois Brick* result was so surprising to all those federal courts, presumably it would have been just as surprising to the 1969 North Carolina legislature. The court recognized a valid policy issue as to litigation complexity versus compensation, but intimated that defendants' concerns were exaggerated:

> It is clear that a suit by indirect purchasers under our antitrust laws will be complex. However, when asked at oral argument whether "chaos reigned" in states which have allowed indirect purchaser suits, defendants were unable to cite a single example. This failure to cite a single indirect purchaser case in which a court has been faced with an impossibly complex suit counsels us that a fear of complexity is not a sufficient reason to disallow a suit by an indirect purchaser, given the intent of the General Assembly to "establish an effective private cause of action for aggrieved consumers of this State."\(^{20}\)

The court evidently viewed the Supreme Court's decision in *Illinois Brick* as counterintuitive, unfair, inconsistent with the legislature's intent to create an effective antitrust remedy for consumers, and hence to be disregarded, despite a number of North Carolina Supreme Court decisions recognizing that federal precedents are persuasive in construing state statutory provisions.

In Massachusetts the U.S. District Court has certified to the Massachusetts Supreme Judicial Court the question whether an indirect purchaser may sue for alleged anticompetitive activity under the Massachusetts Consumer Protection Act,\(^{21}\) even though the plaintiff had conceded that she had no redress under the Massachusetts Antitrust Statute by virtue of *Illinois Brick* and a statutory mandate requiring construction in harmony with federal law.\(^{22}\) The federal court noted that Texas precedent supports defendants' position (the court did not have the benefit of the contrary Florida holding discussed above), but concluded nevertheless


\(\text{\textsuperscript{20}}\) Hyde, 473 S.E.2d at 687–88 (citation omitted).


that predicting the outcome in the Massachusetts courts was just too close to call without guidance from the state's highest court.

Finally, in Tennessee an appellate court has reversed the dismissal of a consumer indirect purchaser class action, holding that, while it was true that the legislature has repeatedly failed to enact an *Illinois Brick* repealer, the "unambiguous provisions" of the state's counterpart of Clayton Act Section 4 made it "abundantly clear" that persons injured by antitrust violations may sue, whether they purchased directly or indirectly. Adding belt to suspenders, the court held that the same result also obtains under the Tennessee Consumer Protection Act because price fixing is most assuredly an "unfair practice."²³

In certain other non-*Illinois Brick* repealer states the news is more of the "dog bites man" variety. Indirect purchasers in Texas are clearly out of luck,²⁴ and recent lower court decisions in Colorado,²⁵ New York,²⁶ and the State of Washington²⁷ have held that in those states (all non-*Illinois Brick* repealer states) there is no antitrust claim by indirect purchasers.²⁸ The New York and Washington decisions are on appeal, however, and in Washington (as in Arizona, where the trial court found that indirect purchasers do have a claim for relief) the attorney general has

²³ Blake v. Abbott Labs., 1996-1 Trade Cas. (CCH) ¶ 71,369 (Tenn. Ct. App. 1996). The court noted in dictum, however, that the complaint was subject to dismissal if it later appears from discovery that "the acts complained of predominantly affect interstate commerce." Id. at 76,858. At least in some states, state actions challenging alleged national or international conspiracies, as distinguished from local home-grown conspiracies, may be vulnerable, in that they exceed the geographic reach, as intended by the legislature, or, possibly, on federal constitutional grounds. Issues relating to extraterritorial application of state antitrust law are beyond the scope of this article.


²⁸ Illinois did enact an *Illinois Brick* repealer, but with the proviso that only the attorney general could institute a class action in state court on behalf of indirect purchasers. 740 ILL. COMP. STAT. ANN. 10/7(2) (West 1992). A recent appellate court decision holds that indirect purchasing consumers unrepresented by the attorney general may not engage in what the court saw as an end run around that restriction by making an antitrust claim under a different statute, the Illinois Consumer Fraud and Deceptive Business Practices Act, 815 ILL. COMP. STAT. ANN. 505/1 et seq. (West 1994). Gaebler v. New Mexico Potash Corp., 1996-2 Trade Cas. (CCH) ¶ 71,659 (III. App. Ct. 1996).
agreed with the plaintiffs in arguing that indirect purchaser actions are permitted under state law.\textsuperscript{29}

Meanwhile, a few lower courts are questioning a proposition that has been conventional wisdom ever since \textit{Illinois Brick}: that if a state does away with the bar to offensive passing-on (in other words, if it lets the indirect purchasers come into court, contrary to \textit{Illinois Brick}), then equity and common sense require that defendants should not be liable under state law to intermediate purchasers for overcharges shown to have been passed on to others.\textsuperscript{30}

To make this rather abstract issue more concrete, let us say that widget manufacturers sell their product to national wholesalers, that sell to local distributors, that sell to retailers, that sell to consumers. Some wholesalers, distributors, and retailers some of the time use widgets as a loss leader—and other middlepersons at other times, for a variety of reasons, do not pass on a price increase immediately. But most intermediaries most of the time sell widgets at their acquisition cost plus a standard markup.

Widget manufacturers are accused of price fixing. Wholesalers sue in a federal class action, as of course they are entitled to do whether or not they passed on the overcharge. Distributors, retailers, and consumers all sue in state court. The question is: in the suits by \textit{retailers and distributors}, may the defendants argue that they are not liable for any overcharge that the retailers merely passed along to their customers?\textsuperscript{31} Opinions in 1996 from the Minnesota Supreme Court\textsuperscript{32} and a Wisconsin trial court,\textsuperscript{33} respectively (both states with \textit{Illinois Brick} repealers), have cast some doubt on the ability of defendants to raise such a defense in a suit by indirect purchasing intermediaries, such as retailers that buy through wholesalers. The Wisconsin opinion relied in part on a 1987 California


\textsuperscript{30} For example, as the proponents of an unsuccessful attempt to repeal \textit{Illinois Brick} at the federal level put it, "multiple liability is fundamentally offensive to notions of simple justice." H.R. REP. No. 95-1397, 95th Cong., 2d Sess. 12 (1978).

\textsuperscript{31} Maybe the price fix resulted in less demand for widgets and the distributors or retailers lost sales as a result, but put that aside and focus instead on whether the manufacturer is liable to the retailer for the overcharge that was passed along from the wholesaler to the distributor to the retailer—and that the retailer in turn passed right along to the consumer.

\textsuperscript{32} Minnesota v. Philip Morris Inc., 551 N.W.2d 490 (Minn. 1996).

\textsuperscript{33} K-S Pharmacies, Inc. v. Abbott Labs., No. 94 CV 2384 (Cir. Ct. Dane Co., Wis. May 17, 1996).
intermediate appellate court decision implying that the question is an open one under the Cartwright Act.34

Despite the opinions cited above, it is too early to say that there is a marked trend toward new exposure at the state level. Most of the recent cases are subject to further appellate review, and defendants have scored some successes, notably on class certification.35 It is, nevertheless, a development worthy of remark when a number of state courts are willing to push the envelope on state antitrust liability.

II. HOW WE GOT HERE

Our judicial system has been wrestling for a very long time with the question of what to do about the economic incidence of an illegal

34 B.W.I. Custom Kitchen v. Owens-Illinois, Inc., 235 Cal. Rptr. 228, 236 (Cal. App. 1987). An ABA monograph suggests that while some states have explicitly elected to repeal Hanover Shoe along with Illinois Brick, a plain-vanilla repealer "presumably leaves Hanover Shoe intact; that is, it does not allow the defendant to claim that the direct-purchaser plaintiff passed the overcharge on to others." ABA SECTION OF ANTITRUST LAW, MONOGRAPH No. 15, ANTITRUST FEDERALISM: THE ROLE OF STATE LAW 29 n.190 (1988). No basis for the presumption is stated, and I respectfully dissent, for such a rule obviously risks duplicative liability. Absent specific legislative history, why would one presume that a legislature intended to create such a result? See Milton Handler & Michael D. Blechman, Antitrust and the Consumer Interest: The Fallacy of Pares Paryiae and a Suggested New Approach, 85 YALE L.J. 626, 649 (1976) ("There appears to be a consensus among all courts that have considered the matter that the problems of proving pass-on must be handled in such a way as to avoid duplicative recoveries for the same alleged overcharge.").

35 Recent indirect purchaser class certification decisions include the following:


Kansas: Donelan V. Abbott Labs., No. 94 C 709 (Dist. Ct. Sedgwick Co., Kan. May 3, 1995) (Kansas infant formula purchasers, yes);


anticompetitive overcharge passed on, in varying amounts, by the direct purchasers through successive layers of distribution and down to the ultimate consumers. It must be a very difficult problem, in that we have dealt with it so long and—at least at the state antitrust level—so inconclusively.

A. The Early Cases

Back in 1906 the Supreme Court held that the City of Atlanta, which had purchased water pipe directly from members of a water pipe cartel, could sue for damages measured by the difference between the fair market price and the higher price that it actually paid. But, though some view Chattanooga Foundry as a precursor of the Illinois Brick/Hanover Shoe line of cases, no one thought to argue in 1906 that Atlanta had merely passed through the overcharge to its thousands of water customers and, hence, had suffered no cognizable injury.

The first cases of any real significance to raise that issue were the Oil Jobber cases from the 1940s, brought by gasoline middlemen that alleged they had paid higher prices in consequence of the oil companies’ market stabilization activities (for which the government had secured convictions in the celebrated Socony-Vacuum case). Indeed, the jobbers had paid higher prices as a result of the refiners’ activities, but from the courts’ perspective, the jobbers had a little problem as plaintiffs: their acquisition cost was contractually fixed by reference to the prevailing retail price and they were therefore guaranteed a constant margin no matter what their cost of gasoline. Thus, it appeared to the courts, the refiners could have fixed prices to their hearts’ delight and the jobbers would not have been a penny out of pocket. Reasoning, in substance, that injury is injury is injury, and he who has not been injured cannot validly ask a court to award damages, the courts dismissed the jobbers’ claims on the pleadings or summary judgment.

During the succeeding years some other courts came out the same way. But in the Electrical Equipment conspiracy cases the tide turned, as the courts brushed aside defendants’ efforts to take discovery as to whether the plaintiff utilities had passed along to their customers the

56 Chattanooga Foundry & Pipe Works v. City of Atlanta, 203 U.S. 390 (1906).
57 See Clark Oil Co. v. Phillips Petroleum Co., 148 F.2d 580 (8th Cir.), cert. denied, 326 U.S. 734 (1945), and other cases cited therein.
overcharges resulting from defendants' illegal activity. The courts rejected defendants' protests that the utilities were about to earn a windfall through litigation, an argument that drew the rejoinder that defendants had awarded themselves a windfall by conspiring to fix prices and rig bids—and there was no injustice in transferring that windfall to the plaintiffs.

B. Hanover Shoe

Perceiving serious tension in the lower courts as to who could sue for damages for price fixing, the Supreme Court decided to address the question in Hanover Shoe, Inc. v. United Shoe Machinery Corp., where the courts below had taken the no-pass-on defense position. There the plaintiff, a shoe manufacturer, relying on the government's earlier victory against United Shoe in its monopolization case based on United's leasing policy, sued for damages measured by the difference between the amount it paid in rentals and the amount it would have paid absent the unlawful policy.

Urging the courts to adopt the "pragmatic" viewpoint of the Oil Jobber cases—the approach that says, "if you passed it on, then you had no injury-in-fact"—the defendant relied on economic reasoning to argue that such an analysis was particularly appropriate in the case at bar, where the same "overcharge" had been imposed on all the shoe manufacturers and the demand for shoes was "so inelastic that the buyer and his competitors could all increase their prices by the amount of the cost..."
increase without suffering a consequent decline in sales." The Court responded, in a passage that gets right to the heart of the difficulty in allowing litigation on pass-on and allocation of damages among successive tiers of purchasers:

We are not impressed with the argument that sound laws of economics require recognizing this defense. A wide range of factors influence a company's pricing policies. Normally the impact of a single change in the relevant conditions cannot be measured after the fact; indeed a businessman may be unable to state whether, had one fact been different (a single supply less expensive, general economic conditions more buoyant, or the labor market tighter, for example), he would have chosen a different price. Equally difficult to determine, in the real economic world rather than an economist's hypothetical model, is what effect a change in a company's price will have on its total sales. Finally, costs per unit for a different volume of total sales are hard to estimate. Even if it could be shown that the buyer raised his price in response to, and in the amount of, the overcharge and that his margin of profit and total sales had not thereafter declined, there would remain the nearly insuperable difficulty of demonstrating that the particular plaintiff could or would not have raised his prices absent the overcharge or maintained the higher price had the overcharge been discontinued. Because establishing the applicability of the passing-on defense would require a convincing showing of each of these virtually unascertainable figures, the task would normally prove insurmountable. On the other hand, it is not unlikely that if the existence of the defense is generally confirmed, antitrust defendants will frequently seek to establish its applicability. Treble-damage actions would require additional long and complicated proceedings involving massive evidence and complicated theories.

In addition, if buyers are subjected to the passing-on defense, those who buy from them would also have to meet the challenge that they passed on the higher price to their customers. These ultimate consumers, in today's case the buyers of single pairs of shoes, would have only a tiny stake in a lawsuit and little interest in attempting a class action.45

No one has effectively refuted either the accuracy or the significance of the points made in the first of the two paragraphs quoted above regarding the difficulty of calculating the pass-on and allocating the damages. But there is a big problem with the point made in the second paragraph of the quotation. In 1968, at a time when the modern class action was in its infancy, it was relatively noncontroversial for the Court to say that the direct buyers had the equities on their side and should be permitted to sue without facing a pass-on defense. But suppose, contrary to the premise set forth in the italicized portion of the quotation

44 Hanover Shoe, 392 U.S. at 492.

45 Id. at 492–94 (emphasis added; footnote omitted). The Court went on to state that situations such as a preexisting cost-plus contract might justify an exception to its holding. Id. at 494.
above, that consumers and other indirect purchasers could—and would—effectively pursue their legal remedies through a class action. How is one to weigh and balance the equities to the various categories of purchasers as against one another, and how is one to balance judicial efficiency against the moral claims of those who bear the real incidence of unlawful price fixing, albeit indirectly?

That is the dilemma with which the federal courts grappled for a decade after Hanover Shoe\textsuperscript{46} (and with which many of the states are

\textsuperscript{46} In 1972 the Supreme Court held that the State of Hawaii could not pursue a parens patriae claim against four oil refiners said to have conspired in restraint of trade and, thus, to have damaged the state’s general economy. Hawaii v. Standard Oil Co. of Cal., 405 U.S. 251 (1972). A primary basis for the Court’s concern was fear of “duplicative recovery”—not duplicative claims by Hawaii, on the one hand, and direct buying wholesalers and retailers, on the other, but rather duplicative claims by the State of Hawaii and by individual Hawaiians as “consumers, for which they may recover themselves under [Clayton Act] § 4.” Id. at 264. The Court held that, absent specific congressional direction, it could not infer from the Clayton Act the right of a state to pursue a claim such as Hawaii’s. The Court’s reasoning in Hawaii v. Standard Oil was troublesome and problematic. On the one hand, the Court emphasized antitrust’s goal of protecting the consumer against overcharges—a goal that had seemed impractical four years earlier in Hanover Shoe and was to be deemed unimportant (by comparison with other objectives) five years later in Illinois Brick. But, having proclaimed the importance of consumer protection as an antitrust goal, the Court, ironically, went on to deprive consumers of a procedural mechanism that many thought well adapted to vindicate their interest in being free from the effects of conspiratorial conduct.

Four years later Congress answered this challenge by enacting the Hart-Scott-Rodino Antitrust Improvements Act (HSR), which added a new § 4C to the Clayton Act, 15 U.S.C. § 15c(a)(1), providing that any state attorney general may bring an action in federal district court

as parens patriae on behalf of natural persons residing in such State . . . to secure monetary relief as provided in this section for injury sustained by such natural persons to their property by reason of any violation of [the Sherman Act]. The court shall exclude from the amount of monetary relief awarded in such action any amount of monetary relief (A) which duplicates amounts which have been awarded for the same injury, or (B) which is properly allocable to (i) natural persons who have [opted out], and (ii) any business entity.

Neither Hawaii v. Standard Oil nor Congress’s legislative response directly addresses the question whether consumers who happen to have bought directly from the conspirators stand on a different footing from consumers who bought through intermediaries. Even so, the legislative impulse behind the HSR Act is difficult to square with the thought that vindicating the interests of indirect purchasing consumers ought to take a back seat to other policy objectives—particularly when so high a proportion of the manufactured products we acquire as consumers are bought through retail stores or other intermediaries.

Note further that in the legislation quoted above Congress not only solved the duplicative damages issue identified in Hawaii v. Standard Oil (by establishing a mechanism for consumers to opt out of parens patriae actions) but also directed the courts to deduct which are “properly allocable to . . . any business entity.” That is, of course, tantamount to automatic opt-out from state parens patriae actions by business firms in their capacity as ultimate consumers (e.g., of coffee for the coffee room). Read literally, however, Congress’s language reached further and attempted in a sort of half-hearted, not to say half-baked, manner to deal with the Hanover Shoe pass-on problem. In (A) above, Congress implied that if the intermediary purchasers get to court first, they may collect the entire overcharge,
now wrestling), as they tried to untangle *Hanover Shoe*’s reasoning to determine whether the end of the pass-on defense implied the demise of the pass-on offense as well. The majority view was no, it did not. For example, in 1973 the Ninth Circuit, in the *Western Liquid Asphalt*47 case, held that plaintiff cities, towns, and other entities, which had bought asphalt through contractors at prices allegedly inflated by a manufacturer conspiracy, could pursue claims against the manufacturers.48

Also worthy of particular note is the Second Circuit’s 1971 opinion in *State of West Virginia v. Chas. Pfizer & Co.*,49 addressing the proper disposition of a fund of $100 million offered by defendants to settle price-fixing claims brought by direct and indirect purchasers of antibiotics. There the parties for the various categories of purchasers had ultimately agreed that governments would get $60 million, consumers would get $37 million, and wholesalers and retailers would get a “‘nuisance value’ allocation of $3 million.”50 The district court approved the arrangement, but certain members of the wholesaler/retailer class appealed, arguing, inter alia, that even if they did just pass on the overcharge, under the reasoning of *Hanover Shoe*, they—the wholesalers and retailers—were entitled to the whole $40 million slice of the pie and the consumers should get nothing. The Second Circuit rejected this argument as a matter of law, holding that one ought to distinguish between offensive and defensive passing on.51

The Third Circuit, however, read *Hanover Shoe* differently. In *Mangano v. American Radiator & Standard Sanitary Corp.*52 it held that plaintiff home builders and owners of homes, apartment buildings, and commercial buildings could not make use of offensive pass-on theory to pursue price-

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48 To like effect was a pre-*Hanover Shoe* case, *Armco Steel Corp. v. North Dakota*, 376 F.2d 206 (8th Cir. 1967), upholding the state’s right to recover as indirect purchaser for overcharges on certain products used in its highways.
49 440 F.2d 1079 (2d Cir.), *cert. denied*, 404 U.S. 871 (1971)).
50 440 F.2d at 1084.
51 *Id.* at 1088.
fixing claims against plumbing fixture manufacturers. Observing that plaintiffs were trying to prove "manufacturers' overcharges on the order of ten to twenty dollars for plumbing fixtures used in buildings selling at twenty to thirty thousand dollars," the Third Circuit perceived itself to be faced with the very same "'insuperable difficulty' spoken of by the Supreme Court in the Hanover case, of demonstrating that any manufacturer's overcharge was a *causa sine qua non* of any payment any of them had to make."53

C. ILLINOIS BRICK

In 1977 the Supreme Court decided to consider *Illinois Brick Co. v. State of Illinois*.54 The lawsuit was brought by the State of Illinois and 700 local governmental entities that contended that concrete block manufacturers had fixed prices and sold the price-fixed blocks to masonry contractors who, in turn, resold the blocks to general contractors, who submitted bids for the construction of buildings that were influenced by the unlawfully high upstream prices. The question presented was whether the State could sue to recover for its indirect injuries, even though, under *Hanover Shoe*, the direct-buying masonry contractors would have a claim for the entire overcharge and the manufacturers would be precluded from showing that they had passed it on, in whole or in part.

As the Court saw it, there were basically three conceivable ways of dealing with this issue:

1. The Universal Pass-on Solution:55 overrule *Hanover Shoe* and let any party assert pass-on defensively or offensively, as the case may be,

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53 438 F.2d at 1188. Translating from the Latin, that means the court could not bring itself to believe that someone who paid $30,000 for the building with the price-fixed plumbing would, in the but-for world, have paid a mere $29,990. That thought just did not compute.

There was another little problem, too. Like Carmen Sandiego, it can be tough to find this elusive "ultimate consumer" whom we wish to "compensate" for the upstream conspiracy. Suppose, for the sake of argument, we are reasonably sure that the building owner who actually paid $30,000 really would have received a $10 discount but for the conspiracy. Where does the buck stop—or, more precisely, where do the ten bucks stop? What if the person who bought the building resold it to someone else? What if the owner rents the building? Is the tenant the one who is really out of pocket? And suppose the tenant is itself a business enterprise. Maybe the customers of that business are the "real" victims.

There are many things to be said about this scenario. One is that it is not far-fetched at all. Another is that there comes a point when the attorneys' fees for all of these various levels of indirect purchasers will eat up the amount that even a terrified defendant is willing to pay in settlement, or a court is willing to award as a judgment.


55 The terms employed for the three perceived alternatives are my own invention, but they are intended to capture the Court's thinking.
or as a variation on the Universal Pass-on Solution, the Court might effectively overrule *Hanover Shoe* by confining it to a limited number of economic circumstances;\(^\text{56}\)

(2) at the other extreme, the Absolutely No Pass-on Solution: a strict rule prohibiting inquiry into the pass-on of an anticompetitive overcharge, whether at the instance of a defendant or an indirect purchasing plaintiff; or

(3) the Complex Compromise Solution:

- permit indirect purchasers to sue (i.e., endorse "offensive pass-on theory");
- try to combine claims by direct purchasers and all layers of indirect purchasers in one big litigation, so as to avoid inconsistent outcomes, correctly allocate the damages pie to everyone in the distribution chain, and avoid duplicative damages;
- where everybody is in one big lawsuit, permit defendants to assert a pass-on defense; but
- keep the *Hanover Shoe*/no pass-on defense rule for cases where only the direct purchasers are the plaintiffs.\(^\text{57}\)

Of the possibilities outlined above, the Complex Compromise Solution was popular in a number of quarters. It was, for example, endorsed generally by the vigorous dissent of Justices Brennan, Blackmun, and Marshall in *Illinois Brick*, by the Justice Department as amicus, and by many lower courts,\(^\text{58}\) and it was similar to the approach Congress seemed to have favored several years earlier in providing for parens patriae actions by state attorneys general under the Hart-Scott-Rodino Act.\(^\text{59}\)

The *Illinois Brick* majority, however, was having none of it. The "principal basis," the majority said,

\(^{56}\) In *Illinois Brick* the plaintiff proposed limiting *Hanover Shoe* to "overcharges for capital goods used to manufacture new products." 431 U.S. at 729.

\(^{57}\) The Court entertained another thought as well: just keep the *Hanover Shoe* rule against defensive pass-on theory but let indirect purchasers make unfettered use of offensive pass-on. The Court thought that result, which seems to be exerting some limited appeal today in the state courts, was too absurd to consider, even in an expansive menu of policy options. *Id.* at 730–35.

\(^{58}\) See *Illinois v. Ampress Brick Co.*, 536 F.2d 1163, 1165–66 (7th Cir. 1976) ("The District of Columbia, Second, Fourth, Fifth, and possibly the Sixth Circuits also [i.e., in addition to the Ninth Circuit in *Western Liquid Asphalt* and the Eighth Circuit in *Armco Steel*] seem hospitably inclined to the rule that ultimate purchasers may sue under Section 4 of the Clayton Act to recover damages incurred as a result of a price-fixing conspiracy."); *rev'd sub nom.* *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977).

\(^{59}\) See supra note 46.
for the decision in *Hanover Shoe* was the Court's perception of the uncertainties and difficulties in analyzing price and output decisions "in the real economic world rather than an economist's hypothetical model" . . . and of the costs to the judicial system and the efficient enforcement of the antitrust laws of attempting to reconstruct these decisions in the courtroom.60

Leaving little doubt that judicial efficiency was its "principal concern" as well, the *Illinois Brick* Court observed, in substance, that having the block makers, the masonry contractors, the general contractors, and the building purchasers all in the courtroom at the same time would in itself do nothing to resolve the question of how the trier of fact could efficiently reach a rational decision as to how much had been passed on and to whom.61 In addition, the majority was concerned that the Complex Compromise Solution left open a "serious risk of multiple liability for defendants."62 It was concerned that procedural devices to bring all layers of purchasers within one big lawsuit would not work—or would not work very well—and it said proponents of the Complex Compromise Solution dismissed too blithely the concern that the direct purchasers would rush into court first and collect their judgment or settlement, leaving the defendants on the hook to pay additional damages to successive layers of indirect purchasers.

Having rejected the Complex Compromise Solution, the Court deemed itself confronted with a stark choice between the Universal Pass-on Solution and the Absolutely No Pass-on Solution.63 It elected the Absolutely No Pass-on Solution because it saw no reason to depart from stare decisis because of the concerns with judicial efficiency described above, and because it perceived the Universal Pass-on Solution as providing less incentive for effective private civil antitrust enforcement than the alternative.64

*Illinois Brick*'s majority understood that it was balancing the desirability of compensating injured victims against considerations of efficient en-

60 431 U.S. at 731–32 (citation and footnote omitted).
61 See id. at 740.
62 Id. at 730.
63 The Court dismissed—too glibly, some would argue—the view that different solutions might properly be applied in different economic circumstances. Id. at 743–44.
64 Although I have used the term "Absolutely No Pass-on" as a shorthand way of describing the alternative chosen by the *Illinois Brick* majority, in fact the Court recognized two limited exceptions: (a) a case where a direct purchaser passes on an overcharge to an indirect purchasing plaintiff with a preexisting cost-plus contract, and (b) a case where the direct and indirect purchaser are commonly owned or controlled. Id. at 736 & n.16. Thus, a more accurate but less felicitious description of the result would be to say that the majority embraced the Hardly Ever Any Pass-on Solution.
forcement and efficient administration of justice.65 The majority likewise agreed with the vigorous dissent that its holding was going to come as a big surprise to Congress, where the legislative history of the Hart-Scott-Rodino Act—not to mention the language of new Section 4C of the Clayton Act66—seemed to imply a favorable view of the Complex Compromise Solution. But Congress, the Court observed, had not changed the language of Section 4 of the Clayton Act in the course of adding Section 4C. The Court indicated that if Congress disagreed with the Court's resolution of the matter, Congress could always act again, this time more clearly.67

Not surprisingly, the result in Illinois Brick seriously upset Messrs. Hart, Scott, and Rodino, who were not amused by an opinion that seemed to fly in the face of their legislation and to grant windfalls to middlemen while denying redress to injured consumers. Remedial legislation was introduced immediately. The reasons underlying the failure of this legislative effort are complex,68 as are the issues; the spirited scholarly debate between Harris and Sullivan, who favored repeal, and Landes and Posner, who did not, still repays careful reading.69 The nub of the matter, however, is that while federal legislation to overrule Illinois Brick was popular with state attorneys general and pro-consumer lobbyists, it was unpopular with business, it was unpopular with defense counsel, and it was unpopular with many plaintiffs' counsel, among whom there was widespread, if not universal, agreement with the Illinois Brick majority's view that giving the whole damages pie to the direct purchasers best motivates the private attorneys general.

In short, while Illinois Brick was (and is) both counterintuitive to many and politically unattractive, Congress found it impossible to legislate in the absence of a rough consensus among interested groups. It was simply unable to overcome objections from diverse quarters that reintroducing pass-on theory into antitrust litigation would stultify the litigation process, to no one's ultimate benefit.70

65 Id. at 746.
70 As a leading member of the plaintiffs' bar put it,
There the matter has rested at the federal level. Indeed, the federal judiciary’s disinclination to allow pass-on theory into antitrust litigation has increased over the years, as seen in a 1990 Supreme Court case, *Kansas v. Utilicorp United, Inc.* There the Court declined to make an exception for regulated utility plaintiffs that pass on all their costs to their customers, holding that, “even assuming that any economic assumptions underlying the *Illinois Brick* rule might be disproved in a specific case, we think it an unwarranted and counterproductive exercise to litigate a series of exceptions.”

D. State “Illinois Brick Repealer” Legislation

Meanwhile, at least in some states, the political calculus and legislative judgment proved different than that prevailing in Congress. In 1978, shortly after the decision in *Illinois Brick*, California amended the Cartwright Act to provide for antitrust claims by indirect purchasers. Wisconsin joined the “Illinois Brick repealer” bandwagon in 1979, as did New Mexico, the latter with a provision making clear that neither *Hanover Shoe* nor *Illinois Brick* would govern in that state. Illinois signed on that year as well, with a provision permitting indirect purchasers to sue on a non-class basis, but with the attorney general as the exclusive representa-

I have to say that the important thing to me is *Hanover Shoe*, *Illinois Brick* is not something that appeals to my heart in the sense that I am opposed to *Illinois Brick* because there is something wrong with not allowing a person who has been hurt to collect in the courts.

But if I have to choose between my heart and my head, in this case, I will take my head. My head is *Hanover Shoe*. *Hanover Shoe* says: “We are going to get antitrust enforcement.” *Illinois Brick* says: “The wrong guys may collect.” That is unfortunate.

But I would rather throw the money down the cesspool than not collect it from the wrongdoer.


An ABA Task Force likewise opposed repeal of *Illinois Brick* at the federal level. See Report of the ABA Section of Antitrust Law Task Force to Review Proposed Legislation to Repeal or Modify *Illinois Brick*, 52 Antitrust L.J. 841 (1983). This coincidence of views between the ABA Task Force and many members of the plaintiffs’ bar illustrates the difficulties that anti-*Illinois Brick* congressmen faced in their unsuccessful effort to build a consensus against the Court’s decision.


72 Id. at 217.

73 [Cal. Bus. & Prof. Code § 16750(a)] (West 1987). It is arguable that, in their pre-World War I antitrust statutes, the legislatures of Alabama and Mississippi, with remarkable prescience, anticipated the *Illinois Brick* controversy and elected to side with the dissent. See Ala. Code § 6-5-60 (1993) and Miss. Code Ann. § 75-21-9 (1991) (both referring to “direct or indirect effects” of combines or trusts).


tive of indirect purchaser classes, and with a statutory direction that the
courts should try to avoid duplicative liability.\textsuperscript{76}

South Dakota was next, enacting its \textit{Illinois Brick} repealer in 1980 with
the proviso that "[i]n any subsequent action arising from the same
conduct, the court may take any steps necessary to avoid duplicative
recovery against a defendant"\textsuperscript{77}—a provision likely to benefit defendants
only if the direct-purchasing South Dakotans are foolish enough to sue
in state rather than federal court and if they sleep on their rights while
the indirect purchasers litigate.

During 1980 there was a more elaborate effort to address the problem
in the District of Columbia, whose \textit{Illinois Brick} repealer\textsuperscript{78} attempts to
reduce to statutory form all the elements of the Complex Compromise
Solution that the Court had rejected in \textit{Illinois Brick}—with \textit{Hanover Shoe}
repealed for cases in which direct and indirect purchasers are both
involved,\textsuperscript{79} and general direction to the courts to use procedural devices,
such as transfer, consolidation, and delay, for the sake of avoiding dupli-
cative litigation, duplicative recovery, and unfairness.\textsuperscript{80} These are laud-
able goals, to be sure, but they will be a little tough for the local D.C.
courts to implement if the direct-purchasing Washingtonians, along with
the direct-purchasing South Dakotans, are in federal court suing under
different rules.

In 1982 Maryland acted to permit suits by governmental entities as
indirect purchasers.\textsuperscript{81} Two years later, in 1984, \textit{Illinois Brick} repealers
were enacted in Michigan\textsuperscript{82} and Minnesota,\textsuperscript{83} the latter with the same
proviso as in South Dakota regarding duplicative recovery in subsequent
actions. Kansas joined them in 1985 with a plain-vanilla \textit{Illinois Brick}
repealer.\textsuperscript{84} In 1987 Hawaii enacted a fairly limited \textit{Illinois Brick} repealer,
providing that only the attorney general may bring a class action on
behalf of indirect purchasers\textsuperscript{85} and that parties asserting claims as indirect

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\textsuperscript{76} 740 ILL. COMP. STAT. ANN. 10/7(2) (West 1992).
\textsuperscript{77} S.D. CODIFIED LAWS § 37-1-33 (Michie 1994).
\textsuperscript{78} D.C. CODE ANN. § 28-4509 (1996).
\textsuperscript{79} Id. § 28-4509(b).
\textsuperscript{80} Id. § 28-4509(c).
\textsuperscript{82} MICH. COMP. LAWS § 445.778(2) (West 1989).
\textsuperscript{83} MINN. STAT. ANN. § 325D.57 (West 1995).
\textsuperscript{84} KAN. STAT. ANN. § 50-801(b) (1995).
\textsuperscript{85} HAW. REV. STAT. § 480-14(b)-(c) (1993). Rhode Island has an even more restrictive
\textit{Illinois Brick} repealer, permitting only a parens patriae action by the attorney general, with
the proviso that there may be no relief which duplicates that already accorded for the
same injury. R.I. GEN. LAWS § 6-36-12(g) (1992).
purchasers on an individual (non-class) basis are limited to single damages.\textsuperscript{86}

There was relatively little reported activity under the *Illinois Brick* repealers during the 1980s. California led the way. The issues centered around class certification and, perhaps more importantly, arguments over the "duplicative recovery" question, an issue the California courts danced around. Consider this statement, for example, by an intermediate appellate court in response to defendants' effort to dismiss the complaint:

We need not here discuss the possibility that there may be both a federal common fund and a state common fund, or whether a federal award may be used to offset a state award. The potential for multiple liability in the present case is sheer speculation. . . .

It is not the function of this court to give advisory opinions on how to avoid a potential multiple recovery. We, as others, are confident that when the threat of double recovery occurs, the trial court will fashion relief accordingly.\textsuperscript{87}

In *B.W.I. Custom Kitchen v. Owens-Illinois, Inc.*\textsuperscript{88} the court certified a class of California middlemen indirect purchasers of glass containers suing for the same alleged violation as a federal class of direct purchasers. The defendants' principal argument against certification was that the plaintiffs might have passed along to their purchasers all the overcharge and, hence, there was no showing of common fact of injury, let alone amount of injury. The court responded in a way that cast some doubt on whether California would deem repeal of *Illinois Brick* tantamount to repeal of *Hanover Shoe* as well:

Whether defendants can bar class certification or negate injury by showing plaintiff and the class "passed on" the overcharge is a question that has not been addressed by any California court, and it would be premature to resolve it at this juncture because we do not have an adequate factual record. However, even if a plaintiff has passed on the entire overcharge, he or she is not per se precluded from otherwise proving injury. For example, even though the entire overcharge has been passed on, the plaintiff may have lost a percentage share of the market or otherwise suffered reduced sales.\textsuperscript{89}

In other *Illinois Brick* repealer states, however, the judiciary did not seem so hospitable to the statutes, and plaintiffs had a harder row to hoe than in California.\textsuperscript{90}

\textsuperscript{88} 235 Cal. Rptr. 228 (Cal. App. 1987).
\textsuperscript{89} Id. at 236.
\textsuperscript{90} See Borden, Inc. v. Universal Indus., 88 F.R.D. 708 (N.D. Miss. 1981) (denying class certification of a class of Mississippi indirect sugar purchasers); Keating v. Philip Morris,
E. ARC America

Significantly, while the courts over the years have discussed the problem of apportionment of overcharges down the “Great Chain of Distribution” to the ultimate consumers, such discussion has arisen in the context of motions to dismiss or efforts to certify a class. Thus, judicial thinking in the state cases as to whether it would be “tough” or “easy” to apportion damages has to date consistently exhibited an airy, ethereal quality because there is no published decision in which a court has purported to make such an apportionment.\(^91\) That was true in 1989, when the Supreme Court came to consider the argument over preemption of the *Illinois Brick* repealers in *California v. ARC America*,\(^92\) and it remains true today.

The procedural posture of *ARC America* was similar to that of the Second Circuit’s 1971 decision in *West Virginia v. Pfizer*.\(^93\) The case arose out of claims of a national price-fixing conspiracy by cement manufacturers. In addition to direct purchasers, among the parties to the proceeding were the attorneys general of the states of Alabama, Arizona, California, and Minnesota, suing as parens patriae under their respective states’ antitrust laws to assert claims by indirect purchasers. As in *Pfizer*, certain defendants established a fund of $32 million to settle all claims in the litigation, including those of the four states as parens patriae, subject to the court’s direction as to the allocation of the funds. It is unclear from the opinions of the district court, the Ninth Circuit, and the Supreme Court whether the court was supposed to allocate the funds in accordance with some formula or methodology. In any event, both the district court and the Ninth Circuit agreed with the direct purchasers that the indirect purchasers should get nothing because the statutes under which such claims were brought were preempted by virtue of the principles set forth in *Hanover Shoe* and *Illinois Brick*.\(^94\)


\(^91\) The author is likewise unaware of any unpublished decisions in which a court has decided a litigated issue as to how much illegal overcharge was passed on to an indirect purchaser or indirect purchasing class. To be distinguished are judicial authorities approving class action settlements in which attorneys for various tiers of direct and indirect purchasing classes have sat down together and whacked up the pie to their mutual satisfaction. *See supra* notes 49–51 and *infra* note 113 and accompanying text.

\(^92\) 490 U.S. 93 (1989).

\(^93\) *See supra* notes 49–51 and accompanying text.

Reversing, the Supreme Court began by observing that there is no express preemption of state antitrust law, nor does federal law "occupy the field." That being the case, preemption arises only if state law stands as an obstacle to effecting Congressional purposes. The Court found no such conflict, holding in essence that if the states want to take up the resources of their own courts with pass-on defenses and claims by remote purchasers, that is their affair; such problems do not directly affect the federal courts, nor is a federal court obligated to adjudicate pendent claims if that would prove inefficient.

As to the concern that allowing indirect purchasers to sue under state law could deprive direct purchasers of their incentive to bring federal claims, the Court thought it clear that the states did not intend to prejudice the ability of any federal plaintiff to collect 100 cents on the dollar. The Court was unimpressed with the argument that incentivizing defendants to settle with indirect-purchasing plaintiffs under state law would leave less blood in the turnip for the direct-purchasing federal plaintiffs. The Court sensed that this argument proved too much, in that any obligations paid by a federal defendant to someone other than a federal plaintiff might deplete the defendant's resources. Finally, although guilty defendants might have to pay more than treble damages as a result of differing rules of standing under state and federal law, the Court was unconcerned: if some of the states want to impose more than treble damages on guilty defendants, that is their affair, and interferes with no federal policy.

Following ARC America, two additional states joined the Illinois Brick repealer movement: Maine, with a plain-vanilla version in 1989, and North Dakota in 1991, with language tracking the New Mexico statutory formula that specifically repeals Hanover Shoe as well as Illinois Brick.

III. THE CURRENT MESS

From one perspective, ARC America is not particularly surprising or controversial: though some wish there were a way to preempt state laws

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95 490 U.S. at 101–02.
96 The Court elected not to take seriously any concern that, in the case at bar, letting the state plaintiffs have a piece of a settlement pie of fixed size necessarily meant that the direct purchasers would get less than they otherwise would. To the Court, this seemed merely an artifact of the way the settlement was structured, not a question of constitutional dimension.
97 Id. at 105–06.
permitting suits by indirect purchasers contrary to federal law—e.g., by specific federal legislation to that effect—few believe that ARC America was off beam as a matter of constitutional law. That being said, ARC America still leaves the law in a serious muddle on the pass-on/allocation issues.

The Illinois Brick Court saw three plausible options for resolving the pass-on dilemma: the Universal Pass-on option, the Absolutely No Pass-on option, and the Complex Compromise under which all the direct and indirect purchasers would gather under one litigation tent to sort out who passed on what and to whom. But each of those options is tacitly based on the assumption that all significant antitrust cases will be brought in federal court—not the current situation, in which markedly different rules prevail in federal and some state courts, as a consequence of which there may be powerful economic incentives for some plaintiffs to sue in federal court and some to sue in state court.

What we have now is not the Universal Pass-on option, because defendants may not assert the pass-on defense in federal court—and may even arguably be barred from using a pass-on defense against secondary indirect-purchasing middlepersons in some few state courts.

Nor do we have the Absolutely No Pass-on option, because an indeterminate number of states permit indirect purchasers to use offensive pass-on theory.

And what we have now is surely not the Complex Compromise, because any effort to deprive direct-purchasing federal plaintiffs of their rights under Hanover Shoe, or to bring them under one big litigation tent with the indirect purchasers and sort out the pass-on, or to give defendants a setoff against the direct purchasers for amounts paid in settlement or judgment to the indirect purchasers, or to let state indirect purchasers assert a claim against the federal direct-purchasing plaintiffs, would run headlong into the incentive structure that the Supreme Court set up in Illinois Brick and so zealously guarded in Utilicorp.

What we have is none of these things. What we have instead is a jerry-rigged legal structure with one ad hoc legal solution balanced precariously on the next. It is, moreover, a structure that could evolve into a powerful engine to encourage settlements, regardless of the factual merits of a case. For it is no secret that if the complaint is not dismissed and if the trial court certifies the class, defendants, by and large, are disinclined to take their chances with a jury.
There are exceptions, of course, such as the trial victory by the *Infant Formula* defendants in the Kansas indirect purchaser suit. But history would indicate that defendants generally are willing to pay some price to settle because of (1) the relative ease with which it is still possible to "prove" a "conspiracy"—and the distrust that members of the jury pool may feel toward "big business"; (2) the rule of joint and several liability; (3) the rule that there is no right to contribution among antitrust defendants found to have conspired with one another; (4) the pooling of claims through class actions; and (5) treble damages. To this rather formidable combination of rules and procedures the Supreme Court has added the rule depriving federal defendants of a pass-on defense, thereby enhancing even further the incentive of direct purchasers to roam through corporate files in search of evidence of what the antitrust bar calls "questionable conversations"—and of defendants to settle when the evidence is found.

If a federal case brought under these federal rules and procedures has a settlement value to a defendant of $10 million, then, as a matter of logic, the existence of another discrete set of potential plaintiffs in another jurisdiction does not reduce that settlement value in the federal case to $9 million, or some other number. That is because, under the current structure, the existence of parallel state indirect purchaser actions does nothing either to reduce the risk to the federal defendant or to increase the risk to the federal plaintiff. Therefore, to the extent that in a significant number of jurisdictions state indirect purchaser litigation is pursued vigorously and effectively, the legal exposure of defendants must necessarily increase, as must the overall cost of antitrust litigation.

In the current system, moreover, the existence of a parallel direct purchaser action arguably does nothing either to reduce the defendant's state litigation risk or to increase the risk of the state indirect purchaser plaintiff. To be sure, some jurisdictions have a statutory mandate to avoid duplicative liability, but such legislative directions must have been based on an expectation that Congress would soon act to change *Illinois Brick*. For, as a matter of logic, "avoiding duplicative liability" would require that the federal direct purchasing plaintiff share its recovery with the state indirect purchasing plaintiff (in obvious contravention of the litigation incentive policies laid down in *Illinois Brick*)—or that the state indirect purchaser plaintiffs would be deprived of their right to recover under

state law where there is a federal direct purchaser plaintiff (in derogation of the "pro-consumer" state legislative policy choice underlying the Illinois Brick repealer statutes). There is no way to avoid this dilemma.

In short, there is no doubt that the expansion of rights of indirect purchasers to sue under state law would materially enhance litigation risk to defendants and significantly augment the economic incentive for attorneys representing successive layers of indirect purchasers to file antitrust actions.

Is that a good thing or a bad thing? Should we point with pride to this enhanced rigor in antitrust enforcement? Or should we view with alarm a possible new trend toward unending litigation in American corporate life? This article can supply no definitive answer to these important questions, for there is none, but the analysis properly begins by examining these questions:

(1) Will more state litigation produce more deterrence of antitrust violations?

(2) Will more state litigation lead to increased recovery by ultimate consumers?

(3) How large a price will society have to pay—in increased litigation expense and burden—to obtain the additional deterrence and the additional recovery for ultimate consumers? And is the extra benefit worth the extra cost?

(4) If the comparison of costs and benefits reveals that things appear to be moving in the wrong direction, the question then becomes what to do about it?

There is substantial ground to believe that the answer to the first question is no, enhanced state antitrust exposure will not buy additional deterrence for antitrust violations. The answer is based partly on experience and "feel," and partly on logic. We already have draconian sanctions against formal and informal cartel activity. There is the threat of three years' imprisonment. There is the threat of millions of dollars in fines in federal criminal enforcement. There is the threat of enormous litigation burden and expense through federal direct purchaser class actions. Last but far from least, there is the threat that an unsympathetic jury will award damages to direct purchasers sufficient to bankrupt a defendant.

These are serious threats, indeed. They are, in fact, more than sufficient by themselves to deter most people from illegal conduct. It is true, of course, that they do not deter everyone. One has met executives with an almost touching faith in the ability of legal counsel to extricate them
from any hole they might dig for themselves—people unable, it would seem, to distinguish between defense counsel and Merlin the Magician. But if individuals of that ilk cannot be deterred by potential federal criminal and civil exposure, then nothing will do the job. Two times zero is still zero, and if that is the amount of equity in one’s company left after the federal trial, the state indirect purchaser case will not make the figure any lower.

The answer to the second question—how much real recovery by ultimate consumers results from state indirect purchaser actions—is: it all depends. An increase in state indirect purchaser exposure will produce some additional recoveries for ultimate consumers—sometimes even from companies that actually have violated the antitrust laws. But the beneficial effect on consumers’ pocketbooks will vary widely from one situation to another. For example, in many cases the consumers will have no record of their purchases. As the Circuit Court of Calhoun County, Alabama, put it:

> It is argued that a special master could overcome many of the problems with proof on the issue of damages [to consumer purchasers of infant formula]. However, for the Court to simply declare that it had a fund or anticipated a fund out of which thousands of retail consumers could essentially help themselves by the filing of a form would encourage fraud and perjury, would invite public criticism of the judicial process and would essentially deny the defendants . . . due process by placing these claims all but beyond the reach of effective cross examination.101

Other important factors that will affect the ultimate consumer’s outcome in varying ways from case to case include:

- whether one can find someone who is a plausible candidate for “the ultimate consumer”;102
- how many transactions away the ultimate consumer is from the price fixers;
- whether all those in-between layers of indirect purchasers are represented by aggressive attorneys who will demand their slice of the pie for their clients and themselves; and finally, it goes without saying,
- the competence, zeal, and ethics of counsel who step forward as champions of the ultimate consumer.

As we have seen, back in 1979 a well-known plaintiffs’ attorney spoke of the need to choose between the heart and the head.103 The present

101 Id. at 13.
102 Recall the discussion about Carmen Sandiego and the price-fixed plumbing, supra note 53.
103 See supra note 70.
system does neither. Instead, it permits not only unfettered rein to direct-purchasing plaintiffs at the federal level but may also, in some jurisdictions, afford the opportunity and the incentive for litigation by layer after layer of indirect purchasers.

Sometimes legal history moves in circuitous and illogical ways but arrives at an acceptable end result. Unfortunately, in my opinion, this is not such a case, for the high potential cost of state indirect-purchaser litigation produces zero increased deterrence, with only questionable benefit in terms of real recovery for ultimate consumers.

IV. THE WAY FORWARD

After ARC America came down, the ABA Antitrust Section appointed a task force to consider options for dealing with the problems raised in this article. The Task Force Report\(^\text{104}\) provided a masterful analysis of the issues and a thorough but inconclusive description of the menu of policy options—in essence (1) retain the status quo, (2) have Congress act to preempt state indirect purchaser statutes, or (3) have Congress act to adopt the Complex Compromise Solution, coupled with preemption of contrary state law. The group also considered two less-complete approaches: uniform state legislation or congressional action to address procedural issues. The Task Force presciently stated its belief “that the full effect of ARC America on private antitrust litigation will not be known for several years”\(^\text{105}\)—a time that now appears to be fast approaching—and opined that “if substantial litigation is filed under state indirect purchaser statutes, the business community’s concerns about the issues posed by ARC America will increase.”\(^\text{106}\)

Some situations must get worse before they get better. This is such a situation, and things indeed appear to be getting worse. If and when the situation becomes intolerable, Congress will inevitably take another look at the options outlined in the Task Force Report, which remains essential reading for anyone concerned with this topic.

The neatest, and arguably the most logical, solution is congressional preemption of state indirect purchaser statutes, enacting, in effect, uniform federal and state adoption of the rules of Hanover Shoe and Illinois Brick. It places a severe strain on credulity, however, to believe this option would ever command sufficient political support. Accordingly, if and


\(^{105}\) Id. at 288.

\(^{106}\) Id. at 289.
when Congress chooses to act to bring some coherence into the area of law discussed in this article, presumably the legislative solution will be some variant of the Complex Compromise Solution.107

In the meantime, how should those concerned with efficiency and justice in antitrust enforcement deal with the issues raised by the current lack of congruence between the federal and state rules? My observations are as follows.

A. STATES WITHOUT ILLINOIS BRICK REPEALERS

Courts in states without Illinois Brick repealers should think twice before adopting as a principle of case law a rule which the legislature has declined to accept. Consider North Carolina, for example. There, as we have seen, a state appellate court this year looked back on the significance of the legislature's 1969 amendment expressly permitting consumers to sue under state antitrust law. Observing that the amendment came one year after Hanover Shoe and eight years before Illinois Brick, the court reasoned that the most reliable indicator of legislative intent would be the decisions of the lower federal courts post-Hanover Shoe and pre-Illinois Brick.

That was an insightful way to approach the problem, but the court's answer was more problematic. As we have seen, the majority of courts

107 For example, Congress could leave Hanover Shoe and Illinois Brick intact at the federal level, and the current state of the law could remain unchanged at the state level, except for lawsuits brought under a new antitrust class action rule, providing for

- bifurcation between a phase 1 in which counsel for all direct and indirect purchasers would seek to prove liability and total amount of the overcharge, and a phase 2 in which subclasses comprised of direct purchasers and each tier of indirect purchasers would seek to establish the amount of the pass-through at each level,
- appropriate economic incentives for plaintiffs' counsel prevailing at the first phase, regardless of the result for their specific clients in the second phase, and
- preemption of parallel or subsequent state actions by indirect purchasers, seeking to recover for the same alleged overcharge at issue in the special federal class action.

Such a rule would:

- address the litigation incentive issue that so concerned the Court in Hanover Shoe and Illinois Brick,
- prevent inconsistent decisions in different fora on liability, total overcharge, and amount of pass-on, all of which are distinct possibilities under the present system, and
- reduce the litigation burden and expense inherent in pursuing parallel litigation in federal court and in multiple state courts.

The defense bar will not, of course, welcome such a proposal with open arms. The question is, however, whether it is superior to all other feasible alternatives, including the status quo.
in the early 1970s favored the Complex Compromise Solution, which involved finding a way to get all the layers of direct and indirect purchasers in the same courtroom. Because of subsequent federal case law developments, however, that approach is not a currently viable option for the North Carolina or any other legislature. Thus—assuming arguendo that the key issue is a reconstruction of legislative intent as of 1969—the real question becomes: If the North Carolina legislature had known in 1969 that federal law would evolve so as to bar indirect purchasers from court and to reinforce the ban on federal defendants’ use of pass-on theory, would it have acted to establish a system risking duplicative liability for defendants and affording an incentive for plaintiffs barred from federal court to come into state court instead?

Of course, no one knows. Maybe it would. Maybe it would not. But surely as a matter of logic, the legislature’s repeated failure in the post-Illinois Brick years to take such a step affords some clue as to what the 1969 legislature would have thought had it been gifted with a legal crystal ball with which to gaze eight years into the future and see Illinois Brick over the horizon. Moreover, the North Carolina legislature, like many others, has long acquiesced in case law expressing a strong preference for interpretation of state law in conformity with federal precedent. If, in other words, it is the general intent of the North Carolina legislature that those injured for antitrust violations should receive compensation for their injuries, it would also appear to be the legislature’s intent that state law should be construed in conformity with federal law absent a compelling reason to the contrary.

The counter-argument is that the Supreme Court in Illinois Brick just got it wrong when, contrary to the “plain meaning” of the Clayton Act (and comparable state law), it “arbitrarily” decided that certain plaintiffs could recover nothing despite antitrust violations causing injury in their business or property. As a policy matter, the argument is debatable, but not without force. The key issue, really, is whether, with such a long history of legislative acceptance of the status quo at both the federal and state levels, a state court should not leave the question of change in the hands of the legislative branch, especially where the benefits of change are so problematic.

B. States Permitting Suits by Indirect Purchasers

First, courts in Illinois Brick repealer states should continue to follow their current practice of staying state litigation pending the outcome of the federal direct purchaser action. Moreover, to state what ought to be obvious but sometimes gets lost, the mere fact that a defendant has been
sued does not prove it is guilty, or even afford much of a basis for reasoned speculation as to whether it might be guilty. Where, therefore, there is a risk of duplicative recovery, a state court should seriously consider whether to stay its hand even on preliminary matters, such as class certification, to abide the outcome at the federal level, particularly where there has been no government action resulting in a consent decree or finding of liability.

Second, although the direct purchasers will almost always be in federal court, state courts in Illinois Brick repealer states should strongly encourage bringing all the indirect purchasers under one big litigation tent, to promote judicial efficiency and reduce the risk of inconsistent outcomes on liability or damages.

Third, the courts should be careful to identify accurately the ultimate consumer, and they should focus on compensating the ultimate consumer’s injury (if any), while minimizing windfall rewards to opportunistic intermediary purchaser plaintiffs. Where the direct purchaser passes on most of its injury to its customers—a circumstance many believe to be common in economic life—federal law already gives that direct purchaser quadruple recovery: once from its immediate purchasers and three times from the defendant. Federal policy, as laid down in Illinois Brick and other authorities, tolerates such windfall recoveries by opportunistic plaintiffs in order to provide proper incentives and to simplify litigation. If, however, a state wishes to take the opposite tack and to emphasize the desirability of recovery by ultimate consumers, it should be especially vigilant to prevent opportunistic intermediary purchasers from reaping where they have not sown. Accordingly, the Illinois Brick repealer state should:

- adopt appropriate rules and/or rebuttable presumptions to identify the ultimate consumer;
- permit defendants to plead and attempt to prove the pass-on defense against intermediate purchasers; and

109 For example, one commentator has urged the adoption of the following presumption, among others: "In antitrust suits initiated under state laws that involve public or commercial construction contracts, the buyers for whom the projects were constructed, whether direct or indirect purchasers, should be the preferred parties to recover damages for illegal overcharges." John Cirace, Apportioning Damages Between Direct and Indirect Purchasers in Consolidated Antitrust Suits: ARC America Unravels the Illinois Brick Rule, 35 VILL. L. REV. 283, 318 (1990). The problem of identifying the ultimate consumer (a question I have termed the Carmen Sandiego issue) could benefit from much additional scholarly attention and debate.
• employ appropriate rules and/or rebuttable presumptions to simplify proof of pass-on, consistent with the policy of avoiding windfall recoveries while compensating the truly injured.

Plaintiffs and defendants both play games and call it the search for justice. Let’s say, for example, that I make peas and am unwise enough to enter into a price-fixing conspiracy. I sell my peas to a grocery wholesaler, which resells to a California grocery store, which in turn resells to Mrs. Jones, an individual who likes peas and is acquainted with counsel knowledgeable in the lore of the Cartwright Act.

When Mrs. Jones sues me on behalf of a class of California pea purchasers, her counsel argues that calculating the overcharge is a breeze: “It’s all very simple, because the wholesaler routinely marks up canned goods by a set amount, and so does the retailer. And I know that Mrs. Jones does not have any records of how many cans she bought, from whom, and how much she paid for them, but we can easily extrapolate on the basis of average pea purchases per Californian during the class period.”

“Just a darn minute!” my counsel replies. “The wholesaler may or may not have a ‘rule of thumb’ about markups, but rules of thumb don’t trump the rules of supply and demand. So unless the demand curve the wholesalers face for canned peas is perfectly inelastic—unless it’s perfectly vertical, instead of downward-sloping like most demand curves—a shift in the supply curve resulting from the price fix would move the point of intersection of wholesaler supply and demand up and to the left. That means the wholesalers would sell fewer peas (maybe some buyers would switch to beans), and while most of the increased cost would be passed on, some would be absorbed at the wholesaler level.”

“I know the wholesalers sued in federal court as direct purchasers,” my counsel continues, “but pass-on wasn’t a relevant issue there, so we have got to have some third-party discovery to get at the facts on the slope of the wholesalers’ supply and demand curves. And once we get through there, we have exactly the same issue with the retailer where Mrs. Jones bought the peas, assuming, that is, we have any idea where she shopped. Plus, we’ve got to look at the deals that wholesalers gave to retailers on canned goods, not to mention the question of whether Mrs. Jones’s grocery store used canned peas as a loss leader. It’s all very complicated!”

Well, it is all very complicated, even in a hypothetical like the California pea purchaser case, which is dorically simple compared with a great many distribution patterns. And note that I did not complicate the matter further by introducing the Carmen Sandiego problem—the possibility
that Mrs. Jones might own a restaurant, and the "real victims" might be the patrons (or perhaps the companies that picked up the expense account tabs for the lunches at which the price-fixed peas were served).

Of course, counsel for the pea purchasers will protest that the defense is just trying to make the case complicated to avoid disgorging their ill-gotten gains and compensating Mrs. Jones for the pennies she lost on her peas. Maybe so, but the class plaintiffs' protest is subject to the retort that they are just trying to oversimplify in order to collect money to which they are not entitled. As a matter of logic, rhetorical claims of "undue complication" versus "undue simplification" cancel out each other. The fact is that if we are going to have an indirect purchaser class action on behalf of consumers, then we are going to have to simplify and adopt some rules of thumb, probably in the form of strong but rebuttable presumptions.

For understandable reasons, there has been relatively little scholarly debate in recent years as to how a rational system of indirect purchaser litigation would work. Herbert Hovenkamp has argued for an expansion of the Illinois Brick "cost-plus exception,"110 and John Cirace has given some thought to the matter,111 but apart from these sources one has to go back to the 1979 Robert Harris and Lawrence Sullivan article.112

I hereby call for a renewed scholarly debate on what rebuttable presumptions about pass-on could promote the just and efficient resolution of proceedings involving the allocation of antitrust overcharges among successive tiers of indirect purchasers.

C. Settlements

Defendants should insist on global settlements with both direct and indirect purchasers. With the law in its current posture there is no way to get all the layers of direct and indirect purchasers into the same courtroom. But, as ARC America itself shows, there is no legal obstacle to having them all in the same conference room to settle the litigation. Defendants, thus, should carefully consider whether their interests are best served by dealing with the federal plaintiffs separately, or whether

111 Cirace, supra note 109.

More recent commentary tends to be of the 'tis-and-cain't variety, focusing on whether indirect purchaser suits are a good thing or a bad thing, not on how to administer them if have them we must.
they should insist on one settlement pie for all, as in Pfizer, ARC America, and other proceedings.

One plaintiffs' attorney, for example, has reported how, in the Chicken Antitrust Litigation, the attorneys for four categories of purchasers, representing three layers of direct and indirect purchasers, were able to divide the settlement fund. Legal representation does not come cheaply, of course, and there is some risk that when we find the elusive Ultimate Consumer, she will only be left with a drumstick. But at least the defendant will not have been sliced, diced, and fricasseed.

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113 See minority views of H. Laddie Montague, Jr., ABA Task Force Report, supra note 70, at 861 (providing information on two proceedings in which settlements apportioned recovery among various classes of direct and indirect purchasers, including In re Chicken Antitrust Litig., 699 F.2d 228 (5th Cir. 1982)).