DEPARTMENT OF JUSTICE

Recent Developments in the Jurisprudence of Direct and Indirect Purchasers

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Thank you for inviting me to speak today and for that kind introduction. I've been asked to discuss recent developments in the jurisprudence of direct and indirect purchasers. My talk will proceed in three parts. First, I will briefly provide a bit of background for context. Second, I will analyze recent opinions in this area of law. Finally, I will attempt to predict the future—where the doctrines are heading, pitfalls for the unwary, and key pivot points in upcoming cases.

I. BACKGROUND

A. *Hanover Shoe* and *Illinois Brick*

To set the stage, I hope you'll indulge me in a brief historical detour. Federal antitrust law permits only direct purchasers to bring suits for damages, and allows them to recover the full portion of their damages, regardless of whether they passed on any portion of those damages to someone else. This rule emerged from two Supreme Court decisions: *Hanover Shoe* and *Illinois Brick*.

First, in *Hanover Shoe*,[1] the Court deployed this rule to the benefit of plaintiffs. There, a shoemaker brought monopolization claims against a manufacturer of shoe-making machines. The defendant manufacturer argued that the plaintiff shoemaker shouldn't be able to sue because he wasn't really injured, on the theory that the shoemaker was able to pass on any overcharges to customers in the form of higher priced shoes. The Court rejected that argument, holding that

[1] *Hanover Shoe, Inc. v. United Shoe Mach. Corp.*, 392 U.S. 481 (1968).

a direct purchaser is allowed to recover damages even if it passed on some of those overpayments to its own customers.

The majority opinion, authored by Justice White, identified two main reasons for this decision. First, calculating what portion of the overcharge was passed on to whom would be too difficult.[2] Second, the Court was concerned that a rule allowing indirect purchasers to recover damages would actually *decrease* antitrust enforcement. The theory was that direct purchasers suffer the most concentrated harm and were the most likely to bring suit. If the defendants could use a pass-on defense to whittle away the amount that a direct purchaser could recover, this would diminish the incentives of direct purchasers to bring suit. Each direct purchaser would have little incentive to bring suit.[3] This strikes modern lawyers as odd in light of class action litigation, but that was underdeveloped at that time.[4] So it is not too hard to excuse the Court's underestimation of how prominent class action enforcement would become. But it is interesting that the Court initially viewed the rejection of a pass-on defense as likely to increase, rather than decrease, private antitrust enforcement.

Almost a decade later, in *Illinois Brick*,[5] the Court addressed the inverse of the question in *Hanover Shoe*: can a plaintiff who did not purchase directly from

[2] *Id.* at 493.
[3] *Id.* at 494.
[4] *See, e.g.*, Fed. R. Civ. P. 23 (amended 1966).
[5] *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977).

the antitrust violator still bring suit to recover damages if the overcharges were passed on to him or her? The Court decided that what is good for the goose is good for the gander: this issue had to rise and fall with *Hanover Shoe*. If a defendant cannot rely on a pass-on to lessen its liability to the direct purchaser, plaintiffs should not be permitted to collect damages that were passed on to them. Otherwise, defendants would face double liability.[6] Persuaded that *Hanover Shoe* was appropriately worried about complicated apportionment calculations, the Court refused to overturn that opinion.[7]

As a result of *Hanover Shoe* and *Illinois Brick*, recovery for antitrust damages is concentrated in the hands of the direct purchaser, who can sue for 100% of the overcharge. Or, as it is more commonly phrased, indirect purchasers do not have standing to bring suit for antitrust damages under federal law.

This regime was (and is) controversial. Indeed, many states decided that they still wanted to allow indirect purchaser plaintiffs to recover antitrust damages and began enacting statutes allowing just that under state law. The Supreme Court blessed those statutes from a preemption perspective in its *California v. ARC America* opinion.[8] Today, at least half the states permit at least some claims for

[6] *Id.* at 729-36.
[7] *Id.* at 736-45.
[8] *California v. ARC Am. Corp.*, 490 U.S. 93 (1989).

damages on behalf of indirect purchasers.[9] This development takes away one of the key benefits that the Court thought it was achieving with *Illinois Brick*: providing a streamlined, more manageable process for antitrust suits. Now, instead of a single suit that resolves claims by both direct and indirect purchasers, companies face multiple suits, often in different courts, and still face the risk of duplicative recovery.[10] The Court subsequently remarked in *UtiliCorp*. that it would not admit of case-by-case exceptions,[11] thereby cementing a regime developed over decades through two Supreme Court cases and state law's continued expansive scope. While the Class Action Fairness Act may at least permit defendants to face both direct and indirect purchasers in the same courtroom, that law does not always apply.

The oddities of this piecemeal regime were one of the main reasons that the Antitrust Modernization Commission recommended overturning *Illinois Brick* and *Hanover Shoe*. That Commission was a group of antitrust experts who were tasked in the early 2000s with examining the antitrust laws to determine whether they should be amended. Our current AAG, Makan Delrahim, served on that commission along with several former AAGs. The Commission's ultimate view

[9] Michael A. Lindsay, Overview of State RPM, The Antitrust Source, https://www.americanbar.org/content/dam/aba/publishing/antitrust_source/lindsay_chart.authcheckdam.pdf (Apr. 2017).
[10] *See* William H. Page, *Class Interpleader: The Antitrust Modernization Commission's Recommendation to Overrule* Illinois Brick, 53 ANTITRUST BULL. 725, 728 (2008).
[11] *Kansas v. UtiliCorp United Inc.*, 497 U.S. 199 (1990).

was that "both direct and indirect purchasers" should be permitted "to sue to recover for actual damages from violations of federal antitrust law."[12] The Commission also believed, however, that it was important to protect against double liability by ensuring that the total amount of damages did not exceed the overcharges paid by the direct purchasers.[13] Despite this recommendation, *Illinois Brick* remains good law, although as I'll discuss a little bit later, it's facing renewed attacks.

B. *Apple v. Pepper*

With that as the background, I'll turn to the allegations in the most recent indirect purchaser case, *Apple v. Pepper*.[14] The plaintiff consumers claim that Apple makes apps for its iPhones available only through the App Store. Apple requires developers to set the price that consumers pay, but consumers pay Apple, and only Apple, to access any app that they wish to download. Apple then keeps a 30% commission on all sales. The Supreme Court had to decide whether the consumer is really a direct purchaser from Apple.

I should pause to note that, although this case may have garnered additional attention because of the products at issue, it is really not all that different from myriad types of commercial arrangements. The relationship between distributors,

[12] ANTITRUST MODERNIZATION COMM'N, REPORT AND RECOMMENDATION 267 (2007), https://govinfo.library.unt.edu/amc/report_recommendation/toc.htm.
[13] *Id.*
[14] *Apple Inc. v. Pepper*, 139 S. Ct. 1514 (2019).

GPOs, and manufacturers in the health care space,[15] and the relationships among the players in the concert ticketing space,[16] both are similar in important ways to the App Store system. So we should not let the tendency to focus on the parties and the facts of a particular case obscure the prevalence of this arrangement.

The United States filed an amicus brief in support of Apple, arguing that the plaintiff consumers should be viewed as indirect purchasers and therefore ineligible to sue for damages under the Sherman Act.[17] The Solicitor General's brief argued that the *Illinois Brick* rule was built out of theories of proximate causation. In other words, *Illinois Brick* was not an antitrust-specific rule, but was applying general common law principles of damages to antitrust law.

Applying these standard principles of proximate causation to the case, the United States argued that the consumers should not qualify as "direct purchasers." The key reason the brief relied on is that the app developers set the prices. It is therefore entirely up to the app developers to decide how to respond to Apple's 30% commission. The plaintiffs were injured only if, and to the extent that, developers sought to recover some or all of Apple's commission by increasing the prices of their apps. Thus, the United States argued, it is the app developers who

[15] *Del. Valley Surgical Supply, Inc. v. Johnson & Johnson*, 523 F.3d 1116 (9th Cir. 2008).
[16] *Campos v. Ticketmaster Corp.*, 140 F.3d 1166 (8th Cir. 1998).
[17] Br. for the United States as Amicus Curiae Supporting Pet'r, *Apple v. Pepper*, 139 S. Ct. 1514 (2019).

feel the effect of any overcharge in the first instance, and any harm to consumers is derivative of the harm to the app developers.

The majority soundly rejected the United States' position. In an opinion written by Justice Kavanaugh, and joined by Justices Breyer, Ginsburg, Sotomayor, and Kagan, the Court held that the iPhone users could proceed with their suit as direct purchasers because they paid money directly to Apple. The majority rejected the argument that *Illinois Brick* and *Hanover Shoe* were applying economic principles, instead viewing those cases as providing an easy-to-administer, bright-line rule grounded in the text of the Clayton Act. In its view, the Clayton Act's text that "any person" can recover damages meant just that: "any person." And that principle was consistently interpreted in precedent to mean that the "immediate buyers" from an antitrust violator could sue under the law.[18]

The dissent, written by Justice Gorsuch and joined by the Chief Justice and Justices Thomas and Alito, would have adopted the United States' position. It believed that the app developers' role in setting the price meant that we should treat the iPhone users as direct purchasers from the app developers and indirect purchasers from Apple.

[18] *Apple*, 139 S. Ct. at 1520.

II. ANALYSIS

A. Supreme Court Antitrust Methodology

In a certain sense, one could describe *Apple v. Pepper* as an unremarkable opinion. Justice Kavanaugh took a longstanding precedent that at least much of the antitrust bar had taken to provide a bright-line rule on who could bring suit, and he applied it to the facts of the case as a bright-line rule. In another sense, however, the opinion is newsworthy and reflects something of a reign of the generalists in the interpretation of the antitrust laws.

On my first review of the case, I was struck that the Court had applied ordinary methodological principles to a Supreme Court precedent. The majority started with a review of the text of the statute, and then turned to the existing precedent. We see this mode of analysis all the time. As Justice Kagan once remarked, we are all textualists now.[19]

But, in the antitrust world, it is unusual to ground the analysis in the text of the Sherman Act or the Clayton Act. The Supreme Court routinely recognizes deviations from the literal language of the statute. For example, Section 1 of the Sherman Act prohibits "*[e]very* contract, combination, . . . or conspiracy, in restraint of trade."[20] Yet since *Standard Oil* in 1911, the Supreme Court has been

[19] The Hon. Elena Kagan, Associate Justice, U.S. Supreme Court, Remarks at Harvard Law School, The Antonin Scalia Lecture Series: A Dialogue with Justice Elena Kagan on the Reading of Statutes (Nov. 25, 2015), available at https://www.youtube.com/watch?v=dpEtszFT0Tg.
[20] 15 U.S.C. § 1 (emphasis added).

satisfied that the Sherman Act covers only "undue restraints," and has imposed a "reasonableness" requirement into the statute.[21]

This focus on statutory text is not the only way in which *Apple v. Pepper* applies standard Supreme Court methodologies to antitrust cases. As I mentioned earlier, Justice Kavanaugh was clear that he was applying a bright-line rule. In fact, he uses this phrase 7 times in his 14-page opinion. The Court generally values clarity, and strives to articulate administrable rules. Yet, those of you who have practiced antitrust law for years will know that the argument for bright-line rules is not always successful in antitrust cases. Sometimes it works: the per se rule is a bright line rule and there are various bright line rules throughout antitrust law. But just last year, Justice Thomas began the analysis section of his opinion in *American Express* by quoting *Eastman Kodak* for the proposition that "[l]egal presumptions that rest on formalistic distinctions rather than actual market realities are generally disfavored in antitrust law."[22] Similarly, in his opinion in *FTC v. Actavis*, Justice Breyer rejected a bright-line rule regarding so-called "pay-for-delay" pharmaceutical transactions. Instead, the Court held that district courts could structure the rule-of-reason analysis to include an evaluation of the strength of the patent, the size of any payment, and whether there were justifications for the

[21] *Standard Oil Co. of N.J. v. United States*, 221 U.S. 1, 60 (1911).
[22] *Ohio v. Am. Express Co.*, 138 S. Ct. 2274, 2285 (2018).

payment.[23] These types of considerations—particularly regarding the strength of the patent—are potentially far more complicated and less at home in standard antitrust cases than an economic calculation to apportion damages. Yet, the Court in *Actavis* held that a bright-line rule was not required to avoid them.

B. The Future of *Illinois Brick*

But perhaps the most fascinating takeaway from the opinion is how much Justice Kavanaugh and the majority undermined a precedent that they were reaffirming.

It started from the very beginning of the opinion. By invoking the text of the Clayton Act, which authorizes damages for "any person" injured by a violation, and then proceeding into precedent, the majority implicitly cast precedent as an artificial limitation on the text of the statute. Indeed, the majority even goes so far as to say later in its opinion that the text should trump the precedent if there appears to be a conflict in this very case.[24] That is not a good place to be for a precedent in a textualist era.

Next, the majority systematically demolished all three of the rationales offered for *Illinois Brick*.[25] It refused to countenance the idea, central to *Hanover Shoe* and *Illinois Brick*, that centralizing private enforcement in the direct

[23] *Fed. Trade Comm'n v. Actavis, Inc.*, 570 U.S. 136, 153-58 (2013).
[24] *Apple*, 139 S. Ct. at 1522.
[25] *Id.* at 1524-25.

purchaser is critical. It then brushed off precedent's second rationale for the rule—the complexity of damages calculation—as "hardly unusual." And it dismisses as inapt any concern that there will be disputes among those who claim a right to a common fund.[26] The *Hanover Shoe/Illinois Brick* rule is left looking like an atextualist, un-empirical deviation from modern jurisprudence.

In light of the majority's explication, it is no surprise that the four-justice dissent sends out the bat signal for cases challenging *Illinois Brick* and *Hanover Shoe*. What is more fascinating, though, is that the dissent harvests the idea of overturning those two cases as a pair.[27] Although the Antitrust Modernization Commission sowed that idea a decade ago, it had not yet been reaped.

The second most fascinating takeaway is that the Court has, in nominally reaffirming a precedent, set forth a way for clever antitrust counsel to earn their keep. As the dissent points out, and the majority does not deny, the decision focuses on privity, that is, the contractual relationship (or lack thereof) between an alleged antitrust violator and his alleged victim.[28] But as any good counselor knows, the relationship between different types of companies in an industry is complex. In some industries, manufacturers and distributors tee off in court all the time but suppliers and manufacturers do not, for legal, business, logistical, or

[26] *See generally* Herbert Hovenkamp *et al.*, Antitrust Law ¶ 346k (4th ed.).
[27] *Apple*, 139 S. Ct. at 1531 (Gorsuch, J., dissenting) ("[I]f we are really inclined to overrule *Illinois Brick*, doesn't that mean we must do the same to *Hanover Shoe*?").
[28] *Id.* at 1529 (Gorsuch, J., dissenting).

historical reasons. In other industries, other antagonisms emerge. The majority's decision allows for counseling on the structure of companies' business arrangements to potentially lessen their litigation risk.

C. Supreme Court Practice Takeaways

Before attempting to predict the future, I wanted to pause for three other points of note for the Supreme Court watchers among us. First, there is a bit of an unexpected lineup in this case, with Justice Kavanaugh joining Justices Ginsburg, Breyer, Sotomayor, and Kagan to form a majority opinion based in large part on textualism. The coalition of the opinion thus crosses both ideological and methodological divides. The same is true of the dissent, with Justice Gorsuch, the Chief Justice, and Justices Thomas and Alito forming an opinion based primarily on pragmatism. I think that reinforces that the justices are calling the balls and strikes in this case.[29]

Second, the interaction between the majority and dissent is also something that I found interesting. We see these dueling hypotheticals between Justice Kavanaugh and Justice Gorsuch trying to illustrate why their proposed rule is principled and why the other proposed rule could easily be evaded. This is rare, where both the majority and dissent are throwing back hypotheticals and accusing the other of being overly formalistic. As a practical matter, I think it highlights the

[29] *See* The Hon. John Roberts, Chief Justice, U.S. Supreme Court, Testimony before the Sen. Committee on the Judiciary (Sept. 12, 2005).

importance of advocates framing the issues in appealing ways. We need to give the justices the proper lens through which to view over one hundred years of precedent from industries that may look nothing like the markets we're looking at today.

This brings me to a third takeaway from the opinion, which is notable for what it does not do: it does not treat this as a "tech case" or suggest that antitrust should approach tech firms or digital markets differently than other markets with respect to the direct purchaser issue. The majority opinion recognizes that the app store is different than a traditional vertical distribution arrangement, and it recognizes that there is not a direct parallel to the market in *Illinois Brick*. Still, Justice Kavanaugh applies that precedent to Apple's conduct here. I think it's fair to say that Justice Gorsuch's opinion does the same, although reaching a different conclusion. This suggests that the Supreme Court views antitrust precedent as flexible enough to handle emerging or rapidly evolving industries.

III. UPCOMING ISSUES

Looking forward, I think we're going to see complications develop in a number of areas as long as *Illinois Brick* remains good law.

One of them is in class certification, and that's currently playing out in a couple of cases in the Ninth Circuit. In *Stromberg*, the court certified a litigation

class under California law that includes both direct and indirect purchasers.[30] This class includes non-California residents, some of whom live in a state that does not permit indirect purchasers to recover damages.[31] Similarly, in the lithium ion battery price fixing matter, the district court certified a settlement class that contained indirect purchasers from states that do not permit these individuals to recover antitrust damages.[32] In the *Stromberg* matter, the United States, along with the states of Texas, Louisiana, Oklahoma, Ohio, and Alaska, filed an amicus brief arguing that the district court's decision to certify a class glosses over the important interests that states have in enforcing their sovereign laws.[33] By our research, this is the first time that the United States has filed an amicus brief with any states at any level of court proceeding, which is an important first. We're still waiting for an opinion in *Stromberg*, which is now scheduled for oral argument in the first week of December. But just last week the Ninth Circuit reversed the settlement in the lithium ion battery matter, finding that it had not adequately explained why the class covered indirect purchasers from states that have not

[30] *In re Qualcomm Antitrust Litig.*, 328 F.R.D. 280 (N.D. Cal. 2018).
[31] *See* Herbert Hovenkamp, *State Antitrust in the Federal Scheme*, 58 IND. L.J. 375, 395 (1983) (citing potential nationwide application of California's indirect-purchaser rule in particular and noting that "extraterritorial application of state antitrust law . . . can be offensive to the two-tier, federal-state antitrust enforcement mechanism").
[32] *In re Lithium Ion Batteries Antitrust Litig.*, No. 13-md-2420 (N.D. Cal.).
[33] Br. of the United States *et al.* as Amici Curiae, No. 19-1519, *Stromberg v. Qualcomm* (9th Cir. June 10, 2019), available at https://www.justice.gov/atr/case-document/file/1172016/download.

repealed *Illinois Brick*.[34] This will be an area for business to keep an eye on, as the Chamber of Commerce's brief in *Stromberg* reveals.

Another area to watch is the co-conspirator "exception" to *Illinois Brick*. The Ninth Circuit recently issued an opinion on this topic in the NFL Sunday Ticket case.[35] The plaintiffs in that matter are individuals who wanted to watch NFL games without purchasing the DirecTV Sunday Ticket. The plaintiffs, who were direct purchasers from DirecTV, alleged a series of agreements between DirecTV, the NFL, and its teams. Defendants argued that plaintiffs were not direct purchasers from the NFL or its teams, and so could not recover damages based on these particular agreements. The Ninth Circuit rejected this argument, holding that the co-conspirator exception allowed plaintiffs to recover damages arising out of any of the agreements that were part of the conspiracy. There was a dissent on this issue, and defendants are seeking rehearing en banc.

Later this week, the Seventh Circuit is hearing argument in a similar matter. In *Marion Healthcare,* the plaintiffs challenged a web of contracts between GPOs, medical device manufacturers, distributors, and individual hospitals. The district court dismissed the case on the ground that plaintiff's theory would require it to calculate pass-on damages.[36] The Division filed an amicus brief on appeal arguing

[34] *In re Lithium Ion Batteries Antitrust Litig.*, ---F. App'x----, 2019 WL 4413215 (9th Cir. Sept. 16, 2019).
[35] *In re Nat'l Football League's Sunday Ticket Antitrust Litig.*, 933 F.3d 1136 (9th Cir. 2019).
[36] *Marion Diagnostic Ctr., LLC v. Becton, Dickinson & Co.*, No. 18-cv-1059, 2018 WL 6266751 (S.D. Ill. Nov. 30, 2018).

that *Illinois Brick* does not preclude a damages action by plaintiffs who purchased from a co-conspirator, even if that co-conspirator would otherwise be considered the direct purchaser who is passing on the damages to the plaintiff.[37] Resolution of these pending matters at the Seventh and Ninth Circuit obviously has the potential to alter the scope of *Illinois Brick* going forward. Indeed, it is possible that *Apple* could put pressure on the co-conspirator exception.

Finally, it is worth watching the *Merricks v. Mastercard* case play out in the United Kingdom. The U.K. permits indirect purchasers to collect damages. The EC previously charged MasterCard with restricting price competition between banks by setting default interchange fees. This provided prima facie evidence of anticompetitive conduct, and Merricks filed a class action on the ground that the interchange fees were passed on to the consumers. The trial court originally refused to permit the matter to move forward because it was unconvinced that expert evidence could demonstrate the "pass-on" to consumers. The appellate court reversed, however, saying that the lower court had demanded too much at that stage of proceedings.[38] In the briefs, the parties vigorously disputed how U.S. law on *Illinois Brick* functioned in practice. That may continue in the U.K. Supreme Court. In addition, the way that plaintiffs develop their economic

[37] Br. of the United States as Amicus Curiae in Support of Appellants and Vacatur, No. 18-3735, *Marion v. Becton Dickinson & Co.* (7th Cir. Apr. 25, 2019), available at https://www.justice.gov/atr/case-document/file/1157436/download.
[38] *Merricks v. Mastercard Inc.*, [2019] EWCA Civ 674.

evidence and how the court ultimately rules on the issue of damages may be instructive to how a post–*Illinois Brick* world would look in the United States. At a minimum, it should give us a practical data point to better understand whether *Illinois Brick*'s concerns about complex apportionment issues for pass-on damages should continue to receive significant weight.

* * *

In closing, I'd suggest that the direct purchaser issue is more alive now than it has ever been. The future is uncertain. *Illinois Brick* was nominally reaffirmed. But the foundation has been laid for a subsequent case overturning *Illinois Brick*. This only becomes more likely as the complex issues that are making their way through the Seventh and Ninth Circuit start to work their way up to the Supreme Court. These cases may force the Court to confront precisely the types of complicated questions that *Hanover Shoe* and *Illinois Brick* were trying to avoid.

Thank you.