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BLOG

Antitrust 101: The Indirect Purchaser Rule of Illinois Brick

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Generally speaking, indirect purchasers do not have standing to sue for damages under federal antitrust law – a rule that was first announced by the Supreme Court in *Illinois Brick v. State of Illinois*, 431 U.S. 720 (1977), and that continues to develop today. For purposes of the rule, a direct purchaser is a person or entity who buys the relevant product (*e.g.*, the price-fixed product) directly from the alleged violator. An indirect purchaser buys the product somewhere down the chain, for example, through a middleman. This blog post will discuss the basics of the rule against indirect purchaser standing and its current status.

The Indirect Purchaser Rule's Beginnings

In *Illinois Brick*, the state of Illinois and local government entities sued manufacturers of concrete bricks for alleged price fixing. The government entities, however, did not buy the bricks directly. Instead, the state had hired contractors who, in turn, hired sub-contractors, and it was the sub-contractors who actually purchased the bricks from the defendant-manufacturers. The state and government plaintiffs argued that, despite being so far removed from the original and direct purchaser, they had standing to sue for damages under federal antitrust law because they ultimately paid the alleged overcharge. The Supreme Court disagreed, reasoning that it would be far too complicated for the plaintiffs to trace their damages through such a convoluted supply chain, potentially subjecting defendants to duplicative claims for damages.

The upshot of the decision is that—for the sake of relative simplicity and efficiency in federal courts—indirect purchasers are barred from pursuing money damages under the Sherman Act.

In reality, the situation is not so clean. Indirect purchasers can and do sue in federal court, including for damages, under the laws of the many states (more than 30) that have repealed *Illinois Brick* via statute or judicial decision for purposes of state law. Additionally, courts have recognized certain exceptions to the bar against indirect purchaser standing.

Exceptions to the Indirect Purchaser Rule

The main carve-outs to the rule against indirect purchaser standing are:

- **Cost plus:** where the direct purchaser has a pre-existing fixed quantity "cost plus" contract with an indirect purchaser (*e.g.*, a supplier charges its customers the total cost of production plus a fixed additional amount). The

reason: it is not difficult to trace an overcharge and determine the damages suffered by an indirect purchaser in a cost plus situation.

- **Co-conspirator:** where the direct purchaser is alleged to have been part of the conspiracy. The reason: the direct purchaser has no incentive to sue.
- **Ownership or control:** where the direct purchaser is owned or controlled by the defendant. The reason: the direct purchaser has no incentive to sue.

The ownership or control exception, in particular, has been heavily litigated, including in the context of "transformed products" (another complication to *Illinois Brick*). For example, in *In re Sugar Industry Antitrust Litigation*, 579 F.2d 13 (3d Cir. 1978), a wholesaler of candy sued twelve sugar refineries alleging a conspiracy to fix the price of refined sugar. The wholesaler did not buy refined sugar (as such) from anyone. Instead, it bought finished candy from a division of one of the refineries and from the subsidiary of another. The Third Circuit concluded that the wholesaler was a direct purchaser with standing to sue for damages under federal antitrust law because it made its purchases directly from an entity owned and/or controlled by an alleged conspirator, and that the wholesaler was not transformed into an indirect purchaser just because the product alleged to have been subject to an illegal overcharge was turned into another product (candy). The court reasoned that, on the facts, it should not be overly difficult to calculate the overcharge on the sugar purchased as part of the candy, and that any other outcome in terms of ownership/control "would invite evasion by the simple expedient of inserting a subsidiary between the violator and the first noncontrolled purchaser."[1]

Just two years after *In re Sugar* was decided, the Ninth Circuit also concluded in *Royal Printing Co. v. Kimberly Clark Corp.*, 621 F.2d 323 (9th Cir. 1980) that "*Illinois Brick* does not bar an indirect purchaser's suit where the direct purchaser is a division or subsidiary of a co-conspirator."[2] In that case, indirect purchasers of paper products were allowed standing to sue the paper manufacturers for alleged antitrust violations despite buying the paper products from subsidiaries of the manufacturers. The Ninth Circuit reasoned that, absent such an exception, there would be no direct purchaser with a reason/incentive to sue.

More recently, the Ninth Circuit examined the ownership or control exception in *In re ATM Fee Antitrust Litigation*, 686 F.3d 741 (9th Cir. 2012). In that case, ATM cardholders sought recovery for alleged overcharges on fees related to the use of ATM machines. Basically: when a cardholder puts a Bank A card into an ATM owned by Bank B, Bank A pays an "interchange" fee to Bank B, which plaintiffs alleged was fixed. The cardholders claimed that they paid the interchange fee indirectly down the chain, but fell within *Royal Printing*'s ownership or control exception since the true direct purchasers (the Bank As) were owned or controlled by the ATM owners (meaning there was no viable direct purchaser to bring suit). The court disagreed on the facts, finding the evidence insufficient that the network of ATM owners did, in fact, own or control the card-issuing banks. The court thus "decline[d] to extend the exception noted in *Royal Printing* to situations where the seller does not own or control the direct purchasers, because, after *Royal Printing*, the Supreme Court stated that 'the possibility of allowing an exception, even in rather meritorious circumstances, would undermine the rule.'"[3]

The Eastern District of Michigan more recently confronted a "transformed products" situation holding, as distinguished from *In re Sugar*, that purported direct purchasers of compressors who had only purchased compressors as part of finished refrigerators containing compressors did not have standing (even if they purchased directly from an owned/controlled entity). The court said that downstream purchasers of finished products lack federal antitrust standing, and the only persons with standing to assert federal damages claims are persons who directly purchased the product that was subject to the alleged conspiracy. *In re Refrigerant Compressors Antitrust Litig.*, 795 F. Supp. 2d 647, 654-59 (E.D. Mich. 2011); *but see* *In re Cathode Ray Tube (CRT) Antitrust Litig.*, 911 F. Supp. 2d 857, 868-73 (N.D. Cal. 2012) (holding that purchasers of transformed products from owned/controlled entities could have direct purchaser standing).

Still Evolving: *Apple v. Pepper*

Finally, in *Apple v. Pepper*, 139 S. Ct. 1514 (2019), the Supreme Court recently held in a 5-4 decision that iPhone users who bought apps on Apple's App Store constitute direct purchasers vis-à-vis Apple. The suit alleged Apple's monopolization of the market for iPhone apps and a supracompetitive 30% commission charged to app developers on the sale of apps. Apple argued that iPhone users are indirect purchasers because they purchased the apps –

not from Apple – but from the third-party app developers who set their own prices and used Apple only as a medium. Apple claimed that the iPhone users could have incurred damages only if Apple's alleged overcharge was passed on to them by the app developers – the type of claim prohibited by *Illinois Brick*.

The Court rejected Apple's argument, concluding that the iPhone users were direct purchasers from Apple because "the iPhone owners bought the apps directly from Apple."[4] The Court reasoned that Apple's argument that app developers set their own prices and were passing on any alleged overcharge by Apple to those developers would "provide a roadmap" to "evade antitrust claims by consumers and thereby thwart effective antitrust enforcement."[5]

The dissent heavily criticized the majority's opinion, explaining that the iPhone users were suing under "exactly the kind of 'pass-on theory' *Illinois Brick* rejected."[6] The dissent suggested that the decision would cause Apple to enter into "less efficient" contractual arrangements with its app developers to avoid liability under the antitrust laws.

The decision opens up a whole new category of "direct purchasers" for companies like Apple that "host" apps for purchase on its devices. More broadly, the decision could have consequences for others who offer platform services (ticket brokers, meal ordering applications, travel websites, real estate platforms, or any other online platform) using vendors or other suppliers.

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[1] *Id.* at 19.

[2] *Id.* at 326.

[3] *Id.* at 757.

[4] *Id.* at 1520.

[5] *Id.* at 1523.

[6] *Id.* at 1528.

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