

December 1977

Price-Fixing, Privity, and the Pass-On Problem in Antitrust Treble-Damages Suits: A Suggested Solution

John Cirace

Follow this and additional works at: <https://scholarship.law.wm.edu/wmlr>



Part of the [Antitrust and Trade Regulation Commons](#)

Repository Citation

John Cirace, *Price-Fixing, Privity, and the Pass-On Problem in Antitrust Treble-Damages Suits: A Suggested Solution*, 19 Wm. & Mary L. Rev. 171 (1977), <https://scholarship.law.wm.edu/wmlr/vol19/iss2/2>

ARTICLES

PRICE-FIXING, PRIVITY, AND THE PASS-ON PROBLEM IN ANTITRUST TREBLE-DAMAGES SUITS:
A SUGGESTED SOLUTION

JOHN CIRACE*

More than sixty years after the New York Court of Appeals rejected privity of contract as a defense in products liability cases,¹ the United States Supreme Court permitted a defendant in an antitrust treble-damages suit to assert lack of privity against an ultimate consumer of the defendant's product.² Although the Court's decision in *Illinois Brick Co. v. Illinois*³ produces results that inadequately harmonize the conflicting goals of the antitrust laws, the elimination of these problems will require congressional, rather than judicial, action. The most appropriate means of legislatively balancing the incompatible antitrust policies, however, has not been considered adequately.

In *Illinois Brick* the state of Illinois, on behalf of 700 various governmental entities, brought an action under section 4 of the Clayton

* B.A., Harvard College; J.D., Stanford University; Ph.D., Columbia University. Assistant Professor of Economics, Herbert H. Lehman College of the City University of New York. The author wishes to thank Professor Donald Dewey of Columbia University for his helpful suggestions and criticism.

1. *MacPherson v. Buick Motor Co.*, 217 N.Y. 382, 111 N.E. 1050 (1916). For a history of the cases leading to the breakdown of the privity rule in product liability see E. LEVI, *AN INTRODUCTION TO LEGAL REASONING* 8-27 (1948); H. BERMAN & W. GREINER, *THE NATURE AND FUNCTIONS OF LAW* 482-504 (3d ed. 1972).

2. *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977).

3. *Id.*

Act⁴ alleging that price-fixing in violation of the Sherman Act⁵ by concrete block manufacturers caused illegal overcharges in the prices of public buildings.⁶ The plaintiffs wanted to demonstrate that the illegal overcharge ultimately passed to them through masonry contractors and general contractors. In response, the defendants moved for partial summary judgment on the ground that, as a matter of law, only direct purchasers had standing to sue antitrust violators. The district court granted their motion,⁷ but the Court of Appeals for the Seventh Circuit reversed, holding that indirect purchasers were entitled to prove any injury in fact.⁸ Thus, the Seventh Circuit joined the Second⁹ and Ninth¹⁰ Circuits in allowing plaintiffs to use pass-on theory to show that injuries accruing from antitrust violations passed to them through intermediate purchasers with and without privity.

The Supreme Court granted certiorari¹¹ to resolve a conflict among the courts of appeals¹² over the validity of the offensive use of pass-on theory.¹³ In its opinion the Court, through Justice White, recognized that it had two alternatives: to overrule or narrowly confine to its

4. Section 4 of the Clayton Act, 15 U.S.C. § 15 (1970) provides:

Any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover three fold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.

5. Section 1 of the Sherman Act, 15 U.S.C. § 1 (1970), provides in pertinent part: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. . . ."

6. *Illinois v. Ampress Brick Co.*, 67 F.R.D. 461, 463 (N.D. Ill. 1975).

7. *Id.* at 467-68. The defendants had entered into a pre-trial consent decree, *United States v. Ampress Brick Co.*, 1974-1 Trade Cas. ¶ 75,060 (N.D. Ill. 1974), which, unlike a final judgment or decree of guilt following a criminal or civil trial, is not prima facie evidence of a violation of the antitrust laws in a subsequent treble-damages action. 15 U.S.C. § 16(a) (1970). For text of § 16(a) see note 34 *infra*.

8. *Illinois v. Ampress Brick Co.*, 536 F.2d 1163, 1167 (7th Cir. 1976).

9. *West Virginia v. Chas. Pfizer & Co.*, 440 F.2d 1079 (2d Cir.), *cert. denied*, 404 U.S. 871 (1971).

10. *In re Western Liquid Asphalt Cases*, 487 F.2d 191 (9th Cir. 1973), *cert. denied*, 415 U.S. 919 (1974).

11. 429 U.S. 938 (1976).

12. Compare cases cited notes 8-10 *supra* with *Mangano v. American Radiator & Standard Sanitary Corp.*, 438 F.2d 1187 (3d Cir. 1971), *aff'g per curiam Philadelphia Hous. Auth. v. American Radiator & Standard Sanitary Corp.*, 50 F.R.D. 13 (E.D. Pa. 1970).

13. 431 U.S. at 728.

facts *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*,¹⁴ which invalidated the pass-on defense, or to preclude the plaintiffs from recovering on their pass-on theory.¹⁵ In *Hanover Shoe* the plaintiff shoe manufacturer brought a treble-damages action against United Shoe, which had monopolized the shoe machinery market with a lease-only policy. United Shoe attempted to defend on the ground that the plaintiff, by virtue of an inelastic demand for its product, had been able to pass the illegal overcharge to its customers.¹⁶ *Hanover Shoe* rejected the pass-on defense¹⁷ for two reasons: first, the Court was unwilling to complicate the "already protracted"¹⁸ antitrust treble-damages actions with theoretical attempts to trace the effects of the illegal overcharge through the chain of production and distribution;¹⁹ second, the Court concluded that allowing direct purchasers to sue would prevent antitrust violators from "retain[ing] the fruits of their illegality"²⁰ whereas indirect purchasers, with little stake in the outcome, would have less incentive to sue the wrongdoers.²¹

Hanover Shoe's elimination of the pass-on defense and the Court's initial determination in *Illinois Brick* that the pass-on rule must apply equally to plaintiffs and defendants in antitrust treble-damages actions²² foreclosed the offensive use of pass-on theory. Thus, *Illinois Brick* held that only direct purchasers could sue antitrust violators and that subsequent purchasers, lacking privity of contract, were precluded from proving that an illegal overcharge was passed to them.²³

In addition to the stare decisis problem presented by *Hanover Shoe*, the Supreme Court in *Illinois Brick* attempted to balance several relevant antitrust law policies. These policies included compensating injured parties,²⁴ deterring antitrust violations,²⁵ protecting defendants from multiple liability,²⁶ and defining a manageable legal stand-

14. 392 U.S. 481 (1968).

15. 431 U.S. at 736.

16. 392 U.S. at 491-92.

17. *Id.* at 492.

18. 431 U.S. at 732.

19. 392 U.S. at 492-93.

20. *Id.* at 494.

21. *Id.*

22. 431 U.S. at 728.

23. *Id.* at 735-36.

24. *Id.* at 737-41.

25. *Id.* at 745-47.

26. *Id.* at 735. After *Hanover Shoe* rejected the defensive use of pass-on theory, many commentators, aware of the potential multiple liability of antitrust defendants, proposed procedural solutions to the problem. See, e.g., McGuire, *The Passing-On Defense and the Right of Remote Purchasers to Recover Treble Damages Under Hanover Shoe*, 33 U. PITT. L. REV. 177 (1971); Comment, *Stand-*

ard.²⁷ Total accommodation of these conflicting policies, however, is virtually impossible. Compensating injured parties, for example, often is incompatible with a manageable legal standard because of theoretical problems in the economic analysis of a damage award. In a pass-on situation, this analysis is complicated further because a monopolistic overcharge has cumulatively larger effects as it occurs farther back in the chain of production and distribution. Similarly, the practical problem of measuring the injuries plaintiffs suffer in specific instances is nearly insoluble.²⁸ If courts emphasize deterrence, however, the remedy should be available to the party best able to assert it; thus, deterrence is not necessarily compatible with compensation. If the protection of defendants from multiple liability and the definition of a manageable legal standard are primary concerns, that is, if courts follow a privity rule, compensation and deterrence assuredly will suffer.

Notwithstanding the problems presented by these conflicting policies, *Hanover Shoe* and *Illinois Brick* have left antitrust law in an unfortunate state. A thesis of this Article is that the absolute privity rule inadequately balances the goals of the antitrust laws and that Congress, by legislation, should limit the rule's applicability in a manner that harmonizes the relevant policies more sufficiently. By combining practical considerations of antitrust enforcement as reflected in several pre-*Illinois Brick* lower court decisions considering the pass-on issue²⁹ with conclusions drawn from general economic prin-

ing to Sue in Antitrust Cases: The Offensive Use of Passing-On, 123 U. PA. L. REV. 976 (1975). See also P. AREEDA, ANTITRUST ANALYSIS 74-76 (2d ed. 1974); Note, *The Effect of Hanover Shoe on the Offensive Use of the Passing-On Doctrine*, 46 S. CAL. L. REV. 98 (1972); Comment, *The Defense of "Passing On" in Treble Damage Suits Under the Antitrust Laws*, 70 YALE L.J. 469 (1961).

27. 431 U.S. at 741-45.

28. Richard Posner has argued that a simple damages remedy is insufficient because many antitrust violations are concealable:

Ideally, the damages award in an antitrust case should equal the social costs of the violation divided by the probability of apprehension and successful prosecution. . . . [T]he treble-damage remedy is too rigid. It overdeters in cases where the probability of punishment is higher than 33 percent and underdeters in cases where the probability is lower. The multiple applied to the actual damages should be permitted to vary depending on the particular circumstances of the case.

R. POSNER, ECONOMIC ANALYSIS OF LAW 361 (1972).

29. Pass-on case law is analogous to the products liability decisions that followed *MacPherson v. Buick's* rejection of the privity defense. See generally R. HURSH & H. BAILEY, AMERICAN LAW OF PRODUCTS LIABILITY (2d ed. 1974); P. KEETON & M. SHAP, PRODUCTS AND THE CONSUMER: DEFECTIVE AND DANGEROUS PRODUCTS (1970); D. NOEL & J. PHILLIPS, PRODUCTS LIABILITY IN A NUTSHELL

ciples, Congress can identify plaintiffs for whom preferred, but not exclusive, standing in treble-damages actions should be granted, regardless of privity. As a first step in this analysis, the Article distinguishes the pass-on problem from the related direct-indirect, target area, and speculative damage problems. This discussion is followed by a presentation of the textbook economic theory of the pass-on problem, which is neither novel nor controversial. The interesting question, however, is the role, if any, that economic theory should play in anti-trust litigation. Justice White, writing for the Court in both *Hanover Shoe* and *Illinois Brick*, has addressed this issue; Professor Schaefer has expressed a contrary position.³⁰ Because their analyses present two extremes, neither of which satisfactorily resolves the complications inherent in antitrust litigation, an alternative theory is proposed.

Applying this alternative theory to legal and economic realities necessitates an analysis of the treatment courts have afforded the pass-on issue. Thus, the Article examines several lower court cases decided before *Illinois Brick* that deemed privity as irrelevant to an appropriate resolution of the pass-on problem. This analysis leads to several conclusions that are worthy of congressional consideration: first, when price-fixing has occurred at any vertical level in the chain of production of goods that are specially constructed for and contracted by the buyer, he should be granted standing to sue for treble damages, despite his lack of privity with the manufacturer;³¹ second, when price-fixing by final product manufacturers has occurred in the vertical chain of production and distribution of mass-produced goods, wholesalers may be able to pass-on the overcharge and therefore are inappropriate plaintiffs in treble-damages suits notwithstanding their privity with the price-fixers;³² third, when price-fixing in the vertical chain of mass-produced goods has occurred

(1974). Those cases dealt effectively with the issue of which firms in a vertical chain of production and distribution would be liable for physical harm caused by unavoidable defects in products. For example, in a case in which an airplane crashed because of a defective altimeter, the manufacturer of the completed airplane, rather than the altimeter manufacturer, was held liable for reasons of social policy: the manufacturer of the completed product usually has a deeper pocket than the component manufacturer and may spread the risk more easily, see *Goldberg v. Kollsman Instrument Corp.*, 12 N.Y.2d 432, 191 N.E.2d 81, 240 N.Y.S.2d 592 (1963). Subsequent cases established that the component manufacturer also may be held liable. See, e.g., *B. K. Sweeney Co. v. McQuay-Norris Mfg. Co.*, 30 Colo. App. 134, 489 P.2d 356 (1971); *Penker Constr. Co. v. Finley*, 485 S.W.2d 244 (Ky. 1972).

30. See Schaefer, *Passing-On Theory in Antitrust Treble Damage Actions: An Economic and Legal Analysis*, 16 WM. & MARY L. REV. 883 (1975).

31. See notes 76-100 *infra* & accompanying text.

32. See notes 101-09 *infra* & accompanying text.

below the level of the final product, standing to sue should be granted to the manufacturer of the final product.³³

PASS-ON IN PRICE-FIXING CASES DISTINGUISHED FROM DIRECT-INDIRECT, TARGET AREA, AND SPECULATIVE DAMAGE PROBLEMS

In suits to recover treble damages for price-fixing, proving a violation of the antitrust laws often is easy because section 5(a) of the Clayton Act³⁴ provides that a final judgment³⁵ for the government in an antitrust action is prima facie evidence against the defendant in subsequent actions by other plaintiffs. Similarly, the amount of damages, by antitrust standards, is relatively specific³⁶ and reasonably ascertainable. It is measured by the difference between actual and "competitive" prices multiplied by the number of units bought.

Prior to the establishment of the *Hanover Shoe* and *Illinois Brick* privity requirements, courts could consider evidence identifying the level or levels in the vertical chain of production and distribution that had suffered injury, and the extent of such injury. Pass-on theory in these cases could be used to determine the proper distribution of the damage award. Plaintiffs could use the concept offensively to demonstrate that the injury from illegal overcharges was passed to them by intermediate purchasers. Moreover, defendants could attempt

33. See notes 120-25 *infra* & accompanying text.

34. Section 5(a) of the Clayton Act, 15 U.S.C. § 16(a) (1970), provides in pertinent part:

A final judgment or decree heretofore or hereafter rendered in any civil or criminal proceeding brought by or on behalf of the United States under the antitrust laws to the effect that a defendant has violated said laws shall be prima facie evidence against such defendant in any action or proceeding brought by any other party against such defendant under said laws. . . , as to all matters respecting which said judgment or decree would be an estoppel as between the parties thereto: *Provided*, That this section shall not apply to consent judgments or decrees entered before any testimony has been taken

35. A plea of *nolo contendere*, which can be made only with the court's consent, FED. R. CRIM. P. 11, falls within the consent judgment exception to § 5(a) of the Clayton Act, see note 34 *supra*, and therefore is unavailable as prima facie evidence against the defendant in a subsequent antitrust action. See *Burbank v. General Elec. Co.*, 329 F.2d 825, 833-35 (9th Cir. 1964).

36. See R. POSNER, *ECONOMIC ANALYSIS OF LAW* ch. 25 (1973); Handler & Blechman, *Antitrust and the Consumer Interest: The Fallacy of Parens Patriae and A Suggested New Approach*, 85 YALE L.J. 626, 655-60 (1976); Lanzillotti, *Problems of Proof of Damages in Antitrust Suits*, 16 ANTITRUST BULL. 329 (1971); Pollock, *Automatic Treble Damages and the Passing-On Defense: The Hanover Shoe Decision*, 13 ANTITRUST BULL. 1183, 1210 (1968).

to prove that their direct purchasers suffered no injury, having passed the initial overcharge, in turn, to their customers.

The pass-on problem in price-fixing cases is distinguishable from the question presented in an antitrust action brought by a plaintiff who is outside the vertical chain of production but who claims through a party in the chain. Such a situation, known as the direct-indirect problem, first occurred in *Loeb v. Eastman Kodak Co.*³⁷ In *Loeb* the plaintiff was a stockholder and creditor of a corporation that was forced into bankruptcy by a price-fixing conspiracy. He sued to recover treble damages, alleging as injuries the loss of his stock and the inability to enforce his claim against the defunct corporation. Noting that the conspiracy was directed at the corporation, however, the Third Circuit held that stockholders and creditors suffered only indirect or consequential injuries.³⁸ Concerned with the need to limit the possibility of multiple suits arising from a single antitrust violation, the court determined that the corporation was the proper party to protect the rights of its stockholders.³⁹ Such a result is appropriate when the person, entity, or class designated to bring the antitrust action has incentive to do so and when the damages award ultimately will be allocated properly between the suing party and those claiming through it because of their business relationship.

The rationale of *Loeb* has been applied in other direct-indirect situations. For example, persons working for firms against whom antitrust violations are alleged have been denied standing to sue.⁴⁰ Lessors have been unable to sue for decreased rental payments caused by antitrust violations that have affected their lessees' businesses adversely.⁴¹ Courts also have prevented patent licensors,⁴² materials suppliers,⁴³ and, apparently, franchisors⁴⁴ from suing for economic losses caused

37. 183 F. 704 (3d Cir. 1910).

38. *Id.* at 709.

39. *Id.*

40. *See, e.g.,* Conference of Studio Unions v. Loew's, Inc., 193 F.2d 51 (9th Cir. 1951), *cert. denied*, 342 U.S. 919 (1952); Westmoreland Asbestos Co. v. Johns-Manville Corp., 30 F. Supp. 389 (S.D.N.Y. 1939). *Contra*, Data Digests, Inc. v. Standard & Poor's Corp., 43 F.R.D. 386 (S.D.N.Y. 1967).

41. *See, e.g.,* Lieberthal v. North Country Lanes, Inc., 332 F.2d 269 (2d Cir. 1964); Melrose Realty Co. v. Loew's, Inc., 234 F.2d 518 (3d Cir.), *cert. denied*, 352 U.S. 890 (1956).

42. SCM Corp. v. Radio Corp. of America, 407 F.2d 166 (2d Cir.), *cert. denied*, 395 U.S. 943 (1969); Productive Inventions, Inc. v. Trico Prods. Corp., 224 F.2d 678 (2d Cir. 1955), *cert. denied*, 350 U.S. 936 (1956).

43. Volasco Prods. Co. v. Lloyd A. Fry Roofing Co., 308 F.2d 383 (6th Cir. 1962), *cert. denied*, 372 U.S. 907 (1963); Snow Crest Beverages, Inc. v. Recipe Foods, Inc., 147 F. Supp. 907 (D. Mass. 1956).

44. Billy Baxter, Inc. v. Coca-Cola Co., 431 F.2d 183 (2d Cir. 1970); Nation-

by antitrust violations directed at the businesses of their licensees, customers, or franchisees.

Also distinguishable from pass-on problems in price-fixing litigations are "target area" cases in which plaintiffs in vertically affected markets have no privity with any party in the vertical chain of production. For example, in *Karseal Corp. v. Richfield Oil Corp.*⁴⁵ the defendant oil company required independent service station operators selling its petroleum products to enter into exclusive dealing contracts for the sale of certain automobile accessories sponsored by the defendant. As plaintiff, Karseal alleged that the service station operators would have purchased its automobile polish if they had not been bound by the exclusive contracts. Although neither in the vertical chain of production nor claiming through a party in the vertical chain, Karseal was in a vertical market affected by the defendant's illegal conduct. The Ninth Circuit characterized the issue of Karseal's ability to sue for treble damages by asking whether the plaintiff was "within the 'target area' of Richfield's illegal practices . . . ? Assuming Karseal was 'hit' by the effect of the Richfield antitrust violations, was Karseal 'aimed at' with enough precision to entitle it to maintain a treble damage suit under the Clayton Act?"⁴⁶

This "rifle range" test is difficult to apply in different fact situations, but it reflects the general concern that injuries caused by illegal conduct not specifically directed at the particular plaintiff are speculative. Moreover, a lenient grant of standing to parties outside the vertical chain of production could create virtually unlimited liability for some antitrust defendants. Such a result would introduce an element of overkill into the Clayton Act's policy promoting private enforcement of the antitrust laws.⁴⁷

wide Auto Appraiser Serv. Inc. v. Association of Cas. & Sur. Cos., 382 F.2d 925 (10th Cir. 1967).

45. 221 F.2d 358 (9th Cir. 1955).

46. *Id.* at 362.

47. See note 4 *supra*. See generally *International Rys. of Cent. America v. United Brands Co.*, 358 F. Supp. 1363, 1370 (S.D.N.Y. 1973). The target area test has been adopted by the Second Circuit. *Calderone Enterprises Corp. v. United Artists Theatre Circuit, Inc.*, 454 F.2d 1292 (2d Cir. 1971), *cert. denied*, 406 U.S. 930 (1972). One court has rephrased the target area test by inquiring whether the plaintiff's injury was a reasonably foreseeable consequence of the defendant's illegal conduct. *Mulvey v. Samuel Goldwyn Prods.*, 433 F.2d 1073 (9th Cir. 1970). The inquiry of another court considered whether a company's injuries were arguably within the zone of interests protected by the statute. *Malamud v. Sinclair Oil Corp.*, 521 F.2d 1142, 1151 (6th Cir. 1975). For a general discussion of the antitrust standing problem see Sherman, *Antitrust Standing: From Loeb to Malamud*, 51 N.Y.U.L. Rev. 374 (1976).

A third area distinguishable from pass-on theory, which primarily is concerned with the proper distribution of the damage award, involves the problem of quantifying the actual injuries. Damages are ascertained most easily in situations in which buyers are forced to pay illegal overcharges. Such overcharges result when the defendants have engaged in price-fixing or discrimination or have required their customers to enter into tying or reciprocity agreements. The measurement of damages becomes more speculative when the injured parties include foreclosed competitors. This situation might arise when a tying agreement contained a provision for exclusive dealing, thus creating the target area problem confronted by the court in *Karseal*.⁴⁸ Competitors also may be eliminated illegally in circumstances involving boycotts, monopolies, and horizontal territorial division agreements. Finally, when the antitrust violation involves an illegal merger or general injury to the economy, the amount of damages is most uncertain.⁴⁹

THE ROLE OF ECONOMIC THEORY IN ANTITRUST LITIGATION

The purpose of pass-on theory, then, is to ascertain the most appropriate allocation of an antitrust treble-damages award among various purchasers in the vertical chain of production and distribution. The next inquiry attempts to determine the extent to which economic analysis properly might aid courts in antitrust litigation. An understanding of the economic theory of the pass-on problem is a prerequisite to this discussion.

The Economic Theory of the Pass-on Problem

The economic complexities of the pass-on problem⁵⁰ are illustrated by a price-fixing hypothetical. Assume that the chain of production of a particular product comprises three vertically related industries. For example, industry 1 consists of ball bearing manufacturers; industry 2 consists of wheel manufacturers; and industry 3 consists of automobile manufacturers. Assume also that industries 2 and 3, the intermediate and final product manufacturers, have competitive economic structures and that industry 1, which is in the form of a monopoly,

48. See text accompanying notes 45-47 *supra*.

49. See, e.g., Handler & Blechman, *supra* note 36, at 655-60. See generally Areeda, *Antitrust Violations Without Damage Remedies*, 89 HARV. L. REV. 1127 (1976); Pollock, *The "Injury" and "Causation" Elements of a Treble-Damage Antitrust Action*, 57 NW. U. L. REV. 691 (1963).

50. For discussions of this topic see P. SAMUELSON, *ECONOMICS* 389-91 (10th ed. 1976); M. SPENCER, *CONTEMPORARY ECONOMICS* 346-50 (2d ed. 1974); R. POSNER, *ANTITRUST* 147-49 (1974).

conspiracy, or cartel, is capable of selling ball bearings at monopoly prices to the wheel manufacturers. The economic issue presented is whether and to what extent the wheel manufacturers can pass the monopolistic overcharge⁵¹ to the automobile manufacturers. Its solution depends upon the relative elasticities⁵² of the industrial supply and demand for wheels.

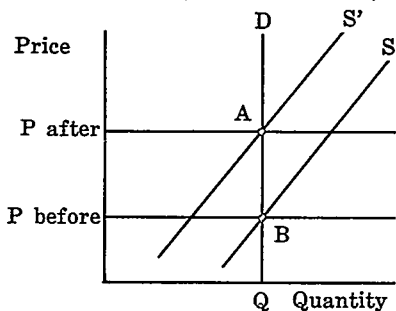
The significance of demand and supply elasticities can be demonstrated by three theoretical cases, two extreme and one general. In terms of the hypothetical described above, one extreme case exists if demand for wheels is totally inelastic (Case 1A) or if the supply of wheels is totally elastic (Case 1B). If the demand for wheels is totally inelastic, automobile manufacturers will purchase the same quantity of wheels regardless of price. If the supply of wheels is totally elastic, wheel manufacturers will supply at a given price all that the market demands and nothing at a lower price. In both situations, wheel manufacturers, as intermediate purchasers, can pass the entire illegal overcharge to automobile manufacturers.⁵³

51. The illegal overcharge resulting from price-fixing is equivalent to a unit tax and can be analyzed in terms of tax incidence theory. *See, e.g.,* R. MUSGRAVE, *THE THEORY OF PUBLIC FINANCE* ch. 13 (1959); R. MUSGRAVE & P. MUSGRAVE, *PUBLIC FINANCE IN THEORY AND PRACTICE* chs. 16, 20 (2d ed. 1976); C. SHOUP, *PUBLIC FINANCE* ch. 10 (1969).

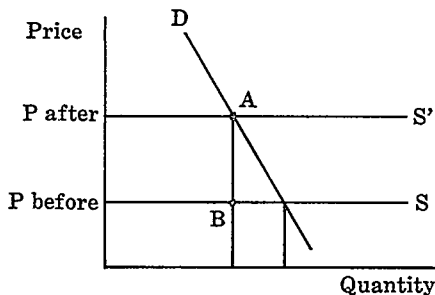
52. Elasticity can be defined as the ratio of the percentage change in quantity demanded or supplied to the percentage change in price. *See* M. SPENCER, *supra* note 50, at 340.

53. This conclusion can be demonstrated by the following illustrations:

CASE 1A (inelastic demand)



CASE 1B (elastic supply)



In both diagrams, supply curve S represents the wheel industry's supply prior to the monopolistic overcharge on ball bearings, and supply curve S' represents the industry's supply curve after the monopolistic overcharge is instituted. The effect of the overcharge is to shift the industry supply curve vertically by AB , the amount of the overcharge per unit. When demand (D) for an intermediate product is totally inelastic, as in Case 1A, consumers of that product will purchase quantity OQ regardless of price. The price after the overcharge, P after, is

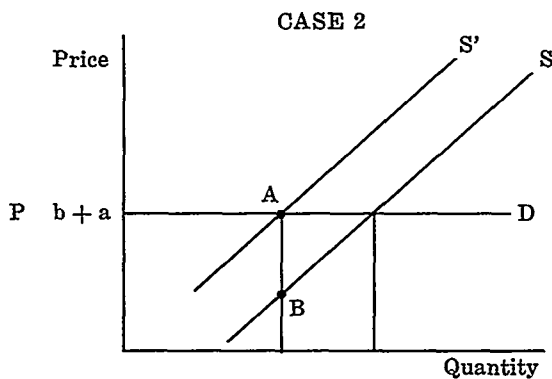
The opposite theoretical extreme (Case 2) would be presented when the demand for wheels was totally elastic. In Case 2 automobile manufacturers would buy all wheels offered at a specific price and nothing at a higher price. As a result, wheel manufacturers could not pass any of the overcharge to automobile manufacturers.⁵⁴

These extreme illustrations, however, rarely exist within a situation involving vertically related industries, such as the present hypothetical. In the general case (Case 3), which reflects economic reality more accurately, neither demand nor supply are completely elastic or inelastic. As a result, some of the overcharge must be borne by the wheel manufacturers and some will be passed to the automobile manufacturers. Similar to the extreme cases, the burdens allocable to each industry will depend on the relative elasticities of supply and demand

higher than the price before, P_{before} , by the entire amount of the overcharge, AB which is passed to the purchasers of the intermediate product.

If an intermediate product's supply curve is totally elastic, as in Case 1B, the manufacturers of that product will supply all that the market desires (D) at a price of P_{before} and nothing at a lower price. The price rises by the total amount of the overcharge, which therefore is passed to the purchasers of the intermediate product. Theoretically, the reduced quantity sold in Case 1B, unlike Case 1A, could place a burden on the intermediate product manufacturers. See M. SPENCER, *supra* note 50, at 348.

54. In Case 2 assume that the wheel industry's supply curve shifts from S to S' by the amount of the monopolistic overcharge, AB .

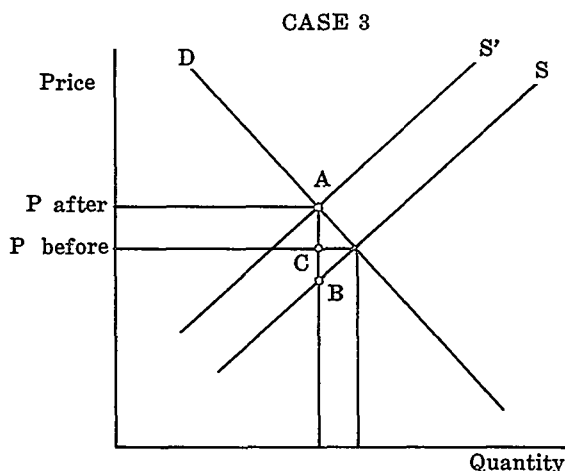


The diagram represents a totally elastic demand (D) for wheels; therefore automobile manufacturers will buy all the wheels offered at price P_{b+a} and nothing at a higher price. Because the price that wheel manufacturers will receive for their product will not reflect the monopolistic overcharge, this industry must bear the entire burden of the antitrust violation. Although the selling price does not rise, the reduced quantity supplied theoretically could place a burden on the automobile manufacturers. See *id.*

for wheels.⁵⁵ Although many factors influence these elasticities, economists, recognizing four general principles, have determined that the demand for a component part of a final product will be less elastic as decreases occur: in the final product's elasticity of demand, in the proportion of the final product's total cost accounted for by that component, in the number of substitutes available for that component, and in the substitute components' elasticity of supply.⁵⁶

Returning to the hypothetical, if wheel manufacturers can pass at least some of the illegal overcharge to automobile manufacturers, a similar analysis must be employed to determine whether automobile manufacturers can pass the overcharge through the chain of distribution to retailers and, ultimately, to consumers.⁵⁷ The analysis be-

55. In the general case neither demand (D) nor supply are totally elastic or inelastic. Assume that supply shifts from S to S' by the amount of the overcharge, AB :



The per unit price paid by automobile manufacturers after the overcharge, P after, is higher than the price before, P before, but only by AC , which is less than the full amount of the monopolistic overcharge, AB . As a result, the wheel manufacturers must absorb BC of the overcharge. See G. STIGLER, *THE THEORY OF PRICE* 17 (rev. ed. 1952).

56. See 5 A. MARSHALL, *PRINCIPLES OF ECONOMICS* ch. 6 (8th ed. 1925); M. SPENCER, *supra* note 50, at 449; G. STIGLER, *THE THEORY OF PRICE* 243 (3d ed. 1966).

57. See, e.g., *Mangano v. American Radiator & Standard Sanitary Corp.*, 438 F.2d 1187 (3d Cir. 1971), *aff'g per curiam Philadelphia Hous. Auth. v. American Radiator & Standard Sanitary Corp.*, 50 F.R.D. 13 (E.D. Pa. 1970), in which manufacturers of plumbing fixtures engaged in price fixing. In dicta the district court considered whether an overcharge paid by wholesalers was passed successively to the plumbing contractors, the general contractors, and, ultimately, the original owners or even the second owners of homes and apartment buildings. For a discussion of *Mangano* see text accompanying notes 126-130 *infra*.

comes more complicated than that described above because a monopolistic overcharge will have cumulative effects as it occurs farther back in the chain of production and distribution. After passing through several stages, the cumulative effect of the overcharge on price per unit may be less than, equal to, or even greater than the initial overcharge.⁵⁸ Unless subsequent stages of production and distribution are perfectly competitive, however, the loss in the value of output at successive stages⁵⁹ is cumulatively larger, with the largest loss experienced at the stage selling the final product.⁶⁰

Economic Pass-on Theory and Antitrust Litigation

Professor Schaefer has suggested that the pass-on problem in antitrust litigation can be resolved by statistical studies and expert testi-

58. If all the subsequent vertically related industries have curves as in Case 2, the price to consumers will not be higher than before the overcharge. If, however, all the subsequent stages have demand and supply curves that are neither totally elastic nor inelastic, as in Case 3, the price will rise cumulatively as an increase in one industry causes an upward shift in the supply curve and a commensurate rise in the price of the next vertically related industry. If the industry demand curves at subsequent stages are relatively elastic and market imperfections are not large, the cumulative rises in price may amount to less than the initial overcharge per unit. If market imperfections in subsequent industries are substantial, the overcharge per unit that consumers pay will be greater than the initial overcharge per unit. For example, successive monopolies in vertically related stages will cause the final price to be higher and the output lower than if only one monopoly existed in the chain of production and distribution. Nevertheless, monopoly profit will be lower: a single monopoly restricts output and raises price so as to maximize profit; a further increase in price caused by a monopoly at a subsequent stage unduly restricts output and therefore produces a reduction in the total profit extracted from consumers. The desire to avoid multiple monopolies in the chain of production and distribution provides a powerful incentive for vertical integration. For discussions of the effects of vertical integration see Adelman, *Integration and Antitrust Policy*, 63 HARV. L. REV. 27 (1949); McGee & Basset, *Vertical Integration Revisited*, 19 J.L. & ECON. 17 (1976); Warren-Boulton, *Vertical Control with Variable Proportions*, 82 J. POL. ECON. 783 (1974).

59. Value of output can be measured as price times quantity sold. Thus, when demand is completely elastic, as in Case 2, price does not rise; nevertheless, the value of output decreases because the overcharge reduces the quantity sold.

60. See McKenzie, *Ideal Output and the Interdependence of Firms*, 61 ECON. J. 785 (1951). As proof of this statement, McKenzie states:

The simplest model . . . is perhaps that where lines of production are isolated from one another but are built up of industries arranged in successive stages. In each stage of production we may suppose that the firms buy productive services from households and intermediate products from the preceding stage. . . . [A]ssume that the factors of production, including intermediate products, may be used in

mony that will estimate the elasticities of demand and supply.⁶¹ Under this rationale, estimates would be necessary for each stage in the chain of production and distribution, and economic theory would be expected to provide a relatively accurate formula for distributing the damage award. Applicable only on a case-by-case basis, Schaefer's position is too simplistic, inasmuch as it suggests that applied economic theory can provide realistic solutions to the pass-on and other problems in antitrust litigation.

The Supreme Court has determined that analyses of economic theories and elasticity studies cannot provide a fully satisfactory solution to antitrust problems. Thus, *Hanover Shoe's* rejection of the pass-on defense manifested the Court's unwillingness to complicate treble-

variable proportions.

... [W]hen the combination of factors is variable, the value of the marginal product of any factor bears the same proportion to the price of the factor that the price of the product bears to the marginal cost. Let us symbolise the average ratio of price to marginal cost in a particular stage of production by ri , where i denotes the stage. Then the withdrawal of a small quantity of a productive service from the i th stage may be expected to reduce the value of the output of that stage by ri times the cost of the services withdrawn. Symbolising the cost of services withdrawn by w , the expected loss is $ri \times w$. This deprives the succeeding stage of intermediate product valued at $ri \times w$. Then by the same argument the decline in output in the $(i + 1)$ th stage will be $ri + 1 \times ri \times w$. Therefore, if price exceeds marginal cost in the subsequent stages of production, the loss in the value of output at successive stages will be cumulatively larger, until the largest loss of all is experienced in the stage producing the final product.

Id. at 789-90.

In addition, the "dead weight" or "welfare loss" resulting from a monopolistic overcharge has cumulatively larger effects at successive stages in the vertical chain of production and distribution. These cumulative effects were suggested to the author by Professor Donald Dewey. For discussions of "dead weight" and "welfare loss" see C. FERGUSON & S. MAURICE, *ECONOMIC ANALYSIS* 287-92 (rev. ed. 1974); W. VICKERY, *MICROSTATICS* 285-88 (1964).

61. Professor Schaefer has stated:

Problems of proof do not present insurmountable obstacles to more liberal standing for remote purchasers. The extent to which an overcharge can be passed on depends upon the elasticity of demand and the elasticity of supply in the market in which the direct purchaser sells. Economists are quite capable of dealing with these subjects; expert witnesses could use numerous statistical techniques that have been developed to measure elasticities of demand and supply. Indeed, estimates of elasticity of demand already have been developed in other contexts for some of the final products the prices of which may have been affected by recent price-fixing conspiracies.

Schaefer, *supra* note 30, at 915-16 (footnotes omitted).

damages actions with theoretical attempts to trace the effects of an illegal overcharge through subsequent purchasers in the chain of production and distribution.⁶² Justice White stated his concern over the introduction of economic intricacies into complex antitrust problems:

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 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. . . . Since establishing the applicability of the passing-on defense would require a convincing showing of . . . virtually unascertainable figures, the task would normally prove insurmountable. On the other hand, . . . if the existence of the defense is generally confirmed, . . . [t]raversable damage actions would often require additional long and complicated proceedings involving massive evidence and complicated theories.⁶³

The problems inherent in calculating the distribution of antitrust damages through the application of economic models rendered the pass-on defense inappropriate. Similar considerations prompted the Court in *Illinois Brick* to reject the pass-on offense:⁶⁴

62. 392 U.S. at 492-93.

63. *Id.* (footnote omitted).

64. Courts and commentators have disagreed on whether *Hanover Shoe* evinced an intention by the Supreme Court to establish an absolute privity requirement. Compare *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 750-53 (Brennan, J., dissenting) and Schaefer, *supra* note 30, at 930 n.195, with Balmac, Inc. v. American Metal Prods. Corp., 1972 Trade Cas. ¶ 74,235, at 93,062 (N.D. Cal. 1972) and *Denver v. American Oil Co.*, 53 F.R.D. 620, 630-31 (D. Colo. 1971). The proposition derives support from *Hanover Shoe's* citation of several precedents, arising under the transportation laws, which discussed the relationship between privity and pass-on. 392 U.S. at 490 & n.8. The first of these was *Southern Pac. Co. v. Darnell-Taenzer Lumber Co.*, 245 U.S. 531 (1918), in which a shipper sought to enforce a reparations order of the Interstate Commerce Commission (ICC) against the defendant railroad. Responding to the defendant's argument that the plaintiffs had suffered no injury because they had passed-on the overcharge, the Court, through Justice Holmes, noted:

The general tendency of the law, in regard to damages at least, is not to go beyond the first step. As it does not attribute remote consequences to a defendant so it holds him liable if proximately the plaintiff has suffered a loss. . . . If it be said that the whole transaction is one from a business point of view, it is enough to reply that the unity in this case is not sufficient to entitle the purchaser to recover, any more than the ultimate consumer who in turn paid an increased price. *He has no privity with the carrier.* . . . The carrier ought not to be allowed to retain his illegal profit, and the only one who can take it from him is the one that alone was in relation with

Under an array of simplifying assumptions, economic theory provides a precise formula for calculating how the overcharge is distributed between the overcharged party (passer) and its customers (passees). . . . Even if these assumptions are accepted, there remains a serious problem of measuring the relevant elasticities. . . . In view of the difficulties that have been encountered, even in informal adversary proceedings, with the statistical techniques used to estimate these concepts, . . . it is unrealistic to think that elasticity studies introduced by expert witnesses will resolve the pass-on issue.⁶⁵

him Behind the technical mode of statement is the consideration well emphasized by the Interstate Commerce Commission, of the endlessness and futility of the effort to follow every transaction to its ultimate result. . . . Probably in the end the public pays the damages in most cases of compensated torts.

Id. at 533-34 (citations omitted) (emphasis supplied). Thus, in *Darnell-Taenzler* Justice Holmes expressed the notion, later adopted by Justice White in *Hanover Shoe*, 392 U.S. at 493, and in *Illinois Brick*, 431 U.S. at 741, that the complications inherent in litigating pass-on issues justified a privity requirement.

Two other early cases that dealt with the pass-on issue were authored by Justice Brandeis, who did not subscribe to Justice Holmes's rigid privity requirement. In *Keogh v. Chicago & Northwestern Ry.*, 260 U.S. 156 (1922), a shipper brought an antitrust action against the defendant railroads, alleging a conspiracy to set unreasonably high rates. Although the Court affirmed a judgment against the shipper because the ICC had approved the rates as reasonable, the opinion ended with dictum that impliedly acknowledged the pass-on defense: "[N]o court or jury could say that, if the rate had been lower, [the plaintiff] would have enjoyed the difference between the rates or that any other advantage would have accrued to him. The benefit might have gone to his customers, or conceivably to the ultimate consumer." *Id.* at 165.

The Court in *Hanover Shoe* distinguished *Keogh* from situations in which a plaintiff would be free to prove an illegal overcharge because the monopolistic prices had not been approved by a legal authority. 392 U.S. at 490 n.8. Likewise, Justice Brandeis subsequently ignored the implications of the *Keogh* dictum when the Court in *Adams v. Mills*, 286 U.S. 397 (1932), again rejected the pass-on defense. The plaintiffs in *Adams* were commission merchants who were engaged in the buying and selling of livestock and who sought enforcement of an ICC reparations order against the stockyard and railroad for excessive rates. Although the merchants had recovered the overcharge from their principals, the livestock owners-shippers, the antitrust violators could not use this fact to limit their damage liability. *Id.* at 407. The remedy for the shippers to whom the excessive rates had been passed lay in subsequent proceedings against the commission merchants. *Id.* at 407-08. Thus, Justice Brandeis apparently accepted the offensive use of pass-on theory. If applied to antitrust treble-damages actions, however, his formulation could discourage private enforcement of the antitrust laws because plaintiffs in privity with a price-fixer might hesitate before establishing themselves as potential defendants in subsequent suits by their direct purchasers.

65. 431 U.S. at 741-42 (footnote omitted).

Thus, in rejecting both the offensive and defensive use of pass-on theory, the Court refused to require that the judiciary resolve treble-damages distribution problems by resorting to strict economic theory, with its necessary simplifying assumptions and statistical quantification difficulties.

Although correct in concluding that elasticity studies cannot resolve the pass-on problem satisfactorily, the Supreme Court unnecessarily adopted a rule of law conflicting with section 4's mandate that anyone injured by antitrust violations may recover treble damages. Moreover, an absolute privity requirement's disregard of economic realities may defeat the goals of the antitrust laws by providing a violator with the distorted economic incentive to structure its business affairs in a manner that insulates it from treble-damages liability. When direct purchasers with privity resell price-fixed goods under a pre-existing, cost-plus contract, for example, they are insulated from antitrust injuries, and the effect of the overcharge is determined in advance. As a result, in *Hanover Shoe* the Court recognized that the pass-on defense might be permitted in such a situation.⁶⁶ Similarly, *Illinois Brick* acknowledged the possible acceptability of the pass-on defense when direct purchasers were owned or controlled by their customers.⁶⁷ In an analogous situation, a manufacturer contemplating a course of action potentially violative of the antitrust laws might create an intermediate dummy firm to insulate itself from treble-damages suits. To deter such action, a court probably would declare that the direct

66. 392 U.S. at 494. See 431 U.S. at 736.

67. 431 U.S. at 736 n.16; cf. *Perkins v. Standard Oil Co.*, 395 U.S. 642 (1969). *Perkins* involved an allegation of price discrimination in violation of § 2(a) of the Robinson-Patman Act, 15 U.S.C. § 13(a) (1970). The defendant sold gasoline at an illegal discount to a firm that resold the gasoline to a subsidiary. In turn, the latter sold to one of its subsidiaries that competed with the plaintiff, a retail service station operator. The Ninth Circuit held that, because the plaintiff competed with a customer of a customer of a party receiving an illegal discount, his injuries were "fourth level" and unprotected by the Act. *Standard Oil Co. v. Perkins*, 396 F.2d 809 (9th Cir. 1968), *rev'd*, 395 U.S. 642 (1969). The Supreme Court reversed because this reasoning would permit price discriminators to avoid the sanctions of the Act merely by adding another link in the chain of distribution. 395 U.S. at 646-48.

The Supreme Court has not determined the extent to which its holdings in *Hanover Shoe* and *Illinois Brick* affect the assertion of pass-on theory in treble-damages actions for Robinson-Patman Act violations. The result in *Perkins* implicitly permitted the assertion of the pass-on offense, and the Court in *Hanover Shoe* suggested that the pass-on defense appropriately might be used in certain cases under the Robinson-Patman Act. 392 U.S. at 494 & n.10.

purchaser was actually a "conduit" for the real purchaser, thus creating yet another exception to the privity rule.⁶⁸

More important than the required judicial exceptions designed to eliminate distorted incentives, however, an inflexible privity requirement may cause a sharp reduction in the deterrent effect of the treble-damages provision in section 4.⁶⁹ *Illinois Brick* has excluded as treble-damages plaintiffs many injured parties who otherwise would have great incentive to sue. A buyer in privity with the antitrust violator, on the other hand, may choose not to sue for a number of reasons: fear of destroying a valuable business relationship; fear of retaliation; indifference because of its ability to pass the overcharge to the next level; lack of funds necessary to engage in antitrust litigation; or aversion to the burden of proving an antitrust violation and the extent of damage suffered.⁷⁰ In addition, *Illinois Brick* conflicts with the Supreme Court's frequent pronouncements that the protection afforded by the antitrust laws should be construed liberally,⁷¹ that antitrust enforcement via "private attorneys general" should be encouraged,⁷² and that defendants should bear the risk of uncertainty in the measurement of damages occasioned by their unlawful actions.⁷³

Despite these countervailing policy considerations, the Court may have justified its adoption of an artificial privity requirement on an erroneous conclusion that simple economic techniques or theories cannot provide guidance for the resolution of antitrust problems. At least one such technique, however, is relevant to antitrust litigation. Stated

68. See *Washington v. General Elec. Co.*, 246 F. Supp. 960, 961 (W.D. Wash. 1965).

69. The Court determined in *Illinois Brick* that the deterrent effect of § 4 is implemented fully if some party brings suit to redress antitrust violations. See 431 U.S. at 746. In establishing the privity requirement, however, the Court gave insufficient consideration both to the reluctance of some direct purchasers to file suit, *id.*, and to the tendency of a monopolistic overcharge to have cumulatively larger effects as it passes through the chain of production and distribution. See notes 58-60 *supra* & accompanying text.

70. See 431 U.S. at 746. See also *In re Western Liquid Asphalt Cases*, 487 F.2d 191, 198 (9th Cir. 1973), *cert. denied*, 415 U.S. 919 (1974); Schaefer, *supra* note 30, at 913-14.

71. Cf. *Perma Life Mufflers, Inc. v. International Parts Corp.*, 392 U.S. 134, 140 (1968) (doctrine of *in pari delicto* not a bar to an antitrust action); *Rado-vitch v. National Football League*, 352 U.S. 445, 454-55 (1957) (courts should not burden private antitrust plaintiff beyond requirements established by Congress); *Mandeville Island Farms, Inc. v. American Crystal Sugar Co.*, 334 U.S. 219, 236 (1948) (Sherman Act protects all potential victims of forbidden practices).

72. See *Hawaii v. Standard Oil Co.*, 405 U.S. 251, 262 (1972).

73. See, e.g., *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 123-24 (1969); *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251, 264-65 (1946).

in a "quasi-general" or "other things being equal" form, economic principles can provide direction in antitrust litigation similar to the guidance furnished by general rules of law. Thus, economic theory can be used to clarify issues, suggest appropriate lines of inquiry, and provide a standard with which to evaluate the costs and benefits of antitrust decisions.⁷⁴ Under this rationale the theoretical extreme pass-on cases and the four principles of elasticity can be useful in establishing and evaluating general rules for antitrust law, even though they cannot resolve precisely specific damages distribution problems.⁷⁵

The recognition of these general rules should demonstrate the inconsistency of an inflexible privity requirement with antitrust policy. Because an overcharge frequently has cumulative effects as it passes through the chain of production and distribution, the goal of compensation often would be served better by preferring ultimate purchasers as plaintiffs over prior purchasers with privity. An absolute adherence to this policy, however, could defeat the other antitrust goals of deterrence, avoidance of multiple liability, and formulation of a manageable legal standard. Therefore, the ultimate rules of standing for antitrust plaintiffs in pass-on cases should reflect a balancing of economic theory and the conflicting antitrust policies.

Before *Illinois Brick's* establishment of the privity requirement, various courts implicitly had employed a balancing approach when resolving standing issues in treble-damages suits. Their decisions suggest strongly that pass-on theory can aid in identifying parties injured by antitrust violations. Clarified by an appreciation of general economic principles, the courts' analyses provide a basis for suggesting three situations in which standing should be granted to certain preferred plaintiffs in order to harmonize the conflicting goals of the antitrust laws.

GENERALIZATIONS SUGGESTED BY PASS-ON LITIGATION

Products Specially Constructed and Contracted for by the Buyer

Many price-fixing cases in which pass-on issues arise concern products specially constructed for and contracted by the buyer. Prior to

74. Principles of oligopoly theory already have contributed to an understanding of the problems accompanying enforcement of the antitrust laws. For an illustration of the ongoing oligopoly theory debate compare Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 HARV. L. REV. 655 (1962), with Posner, *Oligopoly and the Antitrust Laws: A Suggested Approach*, 21 STAN. L. REV. 1562 (1969).

75. For example, the first principle of elasticity, see text accompanying note 56 *supra*, represents the general rule that the more inelastic the demand for the

Illinois Brick several courts had granted these buyers standing to sue for treble damages, producing results more consistent with antitrust policies than are possible under a privity rule. One early case in which privity and pass-on could have been made an issue was *Chattanooga Foundry & Pipe Works v. Atlanta*.⁷⁶ *Chattanooga* was a treble-damages action by the city against two members of the Addyston Pipe conspiracy⁷⁷ for an overcharge on iron pipe. Atlanta purchased pipe pursuant to a contract with a third member of the conspiracy, for use by the city in providing water service to the community. The defendants, however, failed to raise the issues of privity or whether the overcharge had been passed to the city's water customers. Despite the city's lack of privity with the defendants,⁷⁸ the Supreme Court permitted it to sue for treble damages because the illegal overcharge resulting from the conspiracy injured the city financially.⁷⁹

The pass-on issue neglected in *Chattanooga* subsequently was raised by defendants in the *Electrical Equipment Cases*.⁸⁰ These cases were private treble-damages actions brought by utilities against manufacturers who conspired to fix the prices of electrical generators. The affected equipment was purchased either directly by the utilities⁸¹ or by intermediate contractors who incorporated it in projects contracted by the utilities.⁸² In *Commonwealth Edison Co. v. Allis-Chalmers Manufacturing Co.*,⁸³ which involved direct purchases, the Seventh Circuit precluded the defendants from asserting that the plaintiffs

final product, the more inelastic will be the demand for a component part thereof, other things being equal.

76. 203 U.S. 390 (1906).

77. See *Addyston Pipe & Steel Co. v. United States*, 175 U.S. 211 (1899).

78. Atlanta purchased the pipe from Anniston Pipe & Foundry Company, an Alabama corporation, but brought suit against two Tennessee pipe manufacturers. 203 U.S. at 395. The defendants and Atlanta's supplier were members of the Southern Associated Pipe Works trust during the conspiracy.

79. *Id.* at 396. *Accord*, *Thomsen v. Cayser*, 243 U.S. 66, 68 (1917).

80. *E.g.*, *Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co.*, 335 F.2d 203 (7th Cir. 1964); *Washington v. General Elec. Co.*, 246 F. Supp. 960 (W.D. Wash. 1965); *Ohio Valley Elec. Corp. v. General Elec. Co.*, 244 F. Supp. 914 (S.D.N.Y. 1965); *Public Util. Dist. No. 1 v. General Elec. Co.*, 230 F. Supp. 744 (W.D. Wash. 1964); *Atlantic City Elec. Co. v. General Elec. Co.*, 226 F. Supp. 59 (S.D.N.Y.), *appeal denied per curiam*, 337 F.2d 844 (2d Cir. 1964). Over 1,800 treble-damages actions were filed from 1961 to 1963 involving substantially similar facts and collectively referred to as the *Electrical Equipment Cases*. See generally Neal & Goldberg, *The Electrical Equipment Antitrust Cases: Novel Judicial Administration*, 50 A.B.A.J. 621 (1964).

81. *E.g.*, *Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co.*, 335 F.2d 203 (7th Cir. 1964).

82. *E.g.*, *Washington v. General Elec. Co.*, 246 F. Supp. 960 (W.D. Wash. 1965).

83. 335 F.2d 203 (7th Cir. 1964).

had passed the overcharge to their customers.⁸⁴ The court based its holding in part on its prior affirmance of a district court ruling that prevented the Illinois Attorney General from intervening on behalf of electricity consumers.⁸⁵ Indicating that the consumer injury was too remote to permit recovery, the court stated that allowing the passing-on defense "would be tantamount to immunizing defendants from liability."⁸⁶ In *Washington v. General Electric Co.*,⁸⁷ a private contractor had incorporated the electrical equipment into a hydroelectric project. Denying the defendants' motion for summary judgment, the court refused to adopt a privity rule that would have prevented the plaintiff utility from bringing suit to redress the antitrust violation.⁸⁸

The *Electrical Equipment Cases* illustrate the soundness of granting standing in treble-damages suits to purchasers for whom products have been specially constructed or contracted. Both theoretical and practical reasons suggest that the contractors passed on most, if not all, of the overcharge to the utilities. Theoretically, two of the elasticity principles presented in the discussion of the general case support this conclusion.⁸⁹ Because generators are an indispensable component of an electric power project, their demand is highly inelastic. Additionally, because the demand for the residential use of electricity is relatively inelastic,⁹⁰ the demand for generators, a necessary component for the production of electrical power, also is inelastic. From a practical standpoint, as one district court noted, "every

84. *Id.* at 208-09.

85. *Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co.*, 315 F.2d 564 (7th Cir. 1963), *aff'g* 207 F. Supp. 252 (N.D. Ill. 1962).

86. 335 F.2d at 208. *See also* *City of Philadelphia v. Westinghouse Elec. Corp.*, 308 F.2d 856 (3d Cir. 1962), *cert. denied*, 372 U.S. 936 (1963), in which the court prevented the Pennsylvania Public Utility Commission from intervening on behalf of electricity consumers. *Id.* at 860-61. The court correctly refused to grant standing to electricity consumers. To the extent that state regulatory commissions reduced the rate base of each utility to reflect its antitrust recoveries, the overcharge was not passed to consumers. *See* Note, *The Pass-On Defense in Regulated Public Utilities*, 110 U. PA. L. REV. 1113, 1131 (1962). The University of Pennsylvania Law Review mailed a questionnaire to each state's utility regulating agency. The twenty-two responding agencies agreed that a utility recovering treble damages for an equipment overcharge would be required to reduce the carrying value of those assets by the amount of the recovery. *Id.* Even if the rate bases had not been reduced, consumer class actions are inappropriate when the antitrust violations occur beneath the level of the final product. *See* text accompanying notes 120-21 *infra*.

87. 246 F. Supp. 960 (W.D. Wash. 1965).

88. *Id.* at 962.

89. *See* text accompanying note 56 *supra*.

90. *See* C. PHILLIPS, *THE ECONOMICS OF REGULATION* 28-30, 304-05 (1969); C. WILCOX & W. SHEPARD, *PUBLIC POLICIES TOWARD BUSINESS* 410-11 (5th ed. 1975).

manufacturer of goods and services attempts to take into account the cost of equipment and raw materials he buys in setting the price at which he sells his product and, to the extent he succeeds, such costs are passed on."⁹¹ More importantly, in situations when the utility was not a direct purchaser from the generator manufacturer, it had no business relationship to protect, it had no reason to fear retaliation, and it usually could bear the costs and risks of litigation better than the general contractors.

Other cases also provide support for the conclusion that purchasers of specially constructed or contracted products should be granted standing to sue for treble damages. In *Armco Steel Corp. v. North Dakota*,⁹² for example, the defendant steel corporation entered into a conspiracy with three of its distributors to fix the prices of corrugated culverts, structural platepipes, and metal end sections used in highway construction. The products were either purchased directly by the state or included in highway construction projects by private contractors;⁹³ nevertheless, the court of appeals affirmed the district court's damage award providing recovery for both situations.⁹⁴ Despite the state's lack of privity as to all the purchases, the illegal price had been quoted to the private contractors for use in the bids they submitted to the state. Consequently, any overcharge by the manufacturer necessarily was included in the contract prices of the highway projects performed by private builders.⁹⁵

The Court of Appeals for the Ninth Circuit reached a result consistent with *Armco* in *In re Western Liquid Asphalt Cases*.⁹⁶ In that case manufacturers of liquid asphalt engaged in a conspiracy to fix the price of asphalt sold to contractors who used it in combination

91. *Atlantic City Elec. Co. v. General Elec. Co.*, 226 F. Supp. 59, 71 (S.D.N.Y. 1964).

92. 376 F.2d 206 (8th Cir. 1967).

93. *Id.* at 208.

94. *Id.* at 212.

95. *Id.* at 210-11. *Cf. Minnesota v. United States Steel Corp.*, 438 F.2d 1380 (8th Cir. 1971), in which the defendant steel fabricators fixed the price of structural steel that was sold to general contractors and incorporated into road projects built for the state. The defendants' interrogatory inquired whether any overcharge paid by the state was passed to the federal government, which financed up to 90% of the projects' cost. Although the court required an answer to the interrogatory, it noted that the question's relevance depended on whether the increased cost to the contractors had been passed to the state. *Id.* at 1383-85.

96. 487 F.2d 191 (9th Cir. 1973), *cert. denied*, 415 U.S. 919 (1974). *Cf. Standard Indus., Inc. v. Mobil Oil Corp.*, 475 F.2d 220, 224-25 (10th Cir. 1973), *cert. denied*, 414 U.S. 829 (1973) (lower court did not err in permitting jury to consider pass-on defense against general contractor of asphalt roads; nevertheless, the jury found that defendant had not proved its case).

with other ingredients to construct public roads for various states.⁹⁷ Although the district court granted the defendants' motion for summary judgment because the plaintiff states lacked privity,⁹⁸ the Ninth Circuit reversed,⁹⁹ noting that the likelihood of a suit by the contractors was remote and that the states should be permitted to prove their injuries caused by the overcharge.¹⁰⁰

Thus, prior to *Illinois Brick* several courts sensibly had concluded that purchasers of specially constructed or contracted products should be permitted to sue component manufacturers for antitrust violations, regardless of privity. As the analysis of the *Electrical Equipment Cases* demonstrates, these decisions attempted to balance the conflicting goals of the antitrust laws. The courts not only identified those parties most probably injured by the antitrust violations but also granted standing to the plaintiffs with the greatest incentive to bring treble-damages suits. In *Illinois Brick*, on the other hand, the plaintiffs, as purchasers of specially constructed and contracted buildings, sought to recover treble damages from manufacturers of concrete block, a component part of the final product. Inasmuch as these plaintiffs were the most appropriate parties to bring suit, the Supreme Court's holding failed to harmonize the conflicting antitrust policies: its adoption of an artificial privity rule undermined the goals of compensation and deterrence. Hereafter, a purchaser of a specially constructed or contracted product may not redress an illegal overcharge by a component manufacturer unless he has privity with the violator, an issue that many lower courts previously had recognized as irrelevant.

Price-Fixing At or Above the Final Product Level of Mass-Produced Goods

Principles of economics indicate that when price-fixing occurs at or above the level of the final product in the ascending vertical chain of production and distribution of mass-produced goods, ultimate consumers probably will suffer the greatest injury from the illegal overcharge. For example, the supply curves of multiproduct distributors generally are highly elastic;¹⁰¹ therefore, as Case 1B demonstrated above, these distributors will pass-on most of the overcharge.¹⁰² Ac-

97. 487 F.2d at 194-95.

98. *In re Western Liquid Asphalt Cases*, 350 F. Supp. 1369, 1372 (N.D. Cal. 1972).

99. 487 F.2d at 201.

100. *Id.* at 197-99.

101. See C. SHOUP, *supra* note 51, at 274-75; Schaefer, *supra* note 30, at 918-20.

102. See note 53 *supra* & accompanying text. In addition, Case 1A shows that,

cordingly, most wholesalers and retailers of mass-produced goods are inappropriate treble-damages plaintiffs, despite their privity with the price fixers, and a legislative preference should grant standing to institutional consumers and states. As an antitrust plaintiff, a state could bring an action either as a representative of the class of consumers within its borders or as *parens patriae*.

Some courts have recognized that wholesalers and retailers who pass-on illegal overcharges have no valid claim to an antitrust recovery. In the *Oil Jobber Cases*,¹⁰³ for example, the plaintiffs, wholesalers of petroleum products, had privity with the defendant oil refiners. The plaintiffs' profit margins, however, were guaranteed in contracts with the defendants; many plaintiffs actually paid wholesale prices tied to the retail prices of gasoline.¹⁰⁴ In this context the courts accepted the pass-on defense because the plaintiffs were unable to prove injury.¹⁰⁵

A similar result obtained in *West Virginia v. Chas. Pfizer & Co.*,¹⁰⁶ a complex multidistrict combination of sixty-six civil suits alleging that final product manufacturers violated sections 1 and 2 of the Sherman Act in the sale of broad spectrum antibiotic drugs. Among the plaintiffs were various state and local governments, wholesale and retail druggists, institutional consumers such as private hospitals and Blue Cross, and purchasers of antibiotics for non-human purposes. The defendant manufacturer offered \$100 million to settle all claims, and the dispute centered on the appropriate distribution of damages. To resolve this issue, the federal district court divided the plaintiffs into two classes: the first, which consisted of state and local governments and their agencies with claims arising from direct purchases or welfare payments, was awarded \$60 million; the second class, which consisted of wholesalers, retailers, and individual consumers, including

to the extent consumer demand for a commodity is inelastic, total pass-on occurs. *Id.*

103. *Clark Oil Co. v. Phillips Petroleum Co.*, 148 F.2d 580 (8th Cir.), *cert. denied*, 326 U.S. 734 (1945); *Northwestern Oil Co. v. Socony-Vacuum Oil Co.*, 138 F.2d 967 (7th Cir. 1943), *cert. denied*, 321 U.S. 792 (1944); *Twin Ports Oil Co. v. Pure Oil Co.*, 119 F.2d 747 (8th Cir.), *cert. denied*, 314 U.S. 644 (1941); *Leonard v. Socony-Vacuum Oil Co.*, 42 F. Supp. 369 (W.D. Wis.), *appeal dismissed*, 130 F.2d 535 (7th Cir. 1942).

104. *See, e.g., Northwestern Oil Co. v. Socony-Vacuum Oil Co.*, 138 F.2d 967, 969 (7th Cir. 1943), *cert. denied*, 321 U.S. 792 (1944). *See also* *Obron v. Union Camp Corp.*, 477 F.2d 542 (6th Cir. 1973) (pass-on defense permitted against a wholesale distributor who paid manufacturer's list price less 5% but who billed retail customers at manufacturer's list price, thus providing himself with a guaranteed profit margin).

105. *See* cases cited note 103 *supra*.

106. 314 F. Supp. 710 (S.D.N.Y. 1970), *aff'd*, 440 F.2d 1079 (2d Cir.), *cert. denied*, 404 U.S. 871 (1971).

claims of states as *parens patriae* on behalf of their citizens, was awarded the remaining \$40 million. The trial court approved the settlement, which provided that of the \$40 million due the second class only \$3 million would be allocated to wholesalers and retailers as a "nuisance value" and the remainder would be awarded to individual consumers.¹⁰⁷ As direct purchasers the wholesalers maintained that under *Hanover Shoe* they were entitled to the entire \$40 million. The court rejected their claim, however, in part because they sold on a cost-plus basis and in part because of the uncertainty in the law after *Hanover Shoe*.¹⁰⁸

The results in the *Oil Jobber Cases* and in *Chas. Pfizer* clearly comport with practical considerations of antitrust enforcement. A recent study of antitrust actions brought by the government indicates that consumers purchase many items such as bread, dairy products, meat, eggs, and produce, only after those goods have passed through several vertical levels in the chain of distribution.¹⁰⁹ If a price-fixing conspiracy occurs either among manufacturers or wholesalers of a final mass-produced commodity, the privity rule permits the violators to insulate themselves with subsequent distributors from treble-damages suits by ultimate consumers who are most likely to be injured and have an incentive to sue. Wholesalers may be reluctant to sue manufacturers because they hope to maintain business relationships, they lack the financial ability to proceed with a major lawsuit, or they desire to avoid other risks of litigation. Although similar considerations will discourage retailers from suing wholesalers, the size and market power of some chain companies may palliate their natural aversion to seeking an antitrust remedy.

Nevertheless, the problem remains of identifying the most effective plaintiff to protect ultimate consumers' interests when price fixing occurs at or above the final product level of mass-produced goods. If retailers and wholesalers are disqualified from bringing treble-damages suits when price fixing occurs at or above the final product level of mass-produced goods, then consumers must be granted standing to fill the void in antitrust enforcement. In support of the conclusion that the ultimate consumers would be the most effective plaintiffs in these situations, economic theory suggests that the cumulative effects of a monopolistic overcharge passing through the chain of distribution cause the greatest injury to ultimate consumers.

Preferred standing for consumers nevertheless poses many practical obstacles to effective antitrust enforcement. Generally, most con-

107. *Id.* at 728.

108. *Id.* at 745-46.

109. Handler & Blechman, *supra* note 36, at 637.

sumers have too small an interest to file an individual antitrust suit. An exception to this observation, however, exists for institutional consumers, such as hospitals, Blue Cross, and state and local governments, that suffer substantial injury as a consequence of their volume purchasing. These consumers should be granted standing regardless of their lack of privity with defendants. In other situations, class action suits could provide a vehicle for individual consumers to pool their claims in a single suit and to seek recovery for their aggregated injuries. Three mechanisms presently exist for representing consumers in these contexts: individual consumer class actions, class actions brought by states as representatives of similarly situated consumers within its borders, and *parens patriae* actions brought by states on behalf of their resident consumers. Of these options the latter two are preferable to individual consumer class actions.

The distribution of damages to a class containing large numbers of unidentified members creates a major obstacle to effective consumer class actions. In *Eisen v. Carlisle & Jacquelin*,¹¹⁰ for example, the Second Circuit held that a class action could not be maintained on behalf of six million persons, of whom only two million were identifiable, because it was unmanageable.¹¹¹ Similarly, in *Donson Stores v. American Bakeries Co.*¹¹² the representatives of a putative class of twenty million consumers sought to intervene in a treble-damages action brought by retail grocery stores against baking companies for price-fixing. The court, rejecting the would-be consumer representatives' contention that the illegal overcharge had been passed to the ultimate buyers, relied on *Hanover Shoe's* implication that only direct purchasers could bring antitrust treble-damages suits.¹¹³

110. 479 F.2d 1005 (2d Cir. 1973), *vacated*, 417 U.S. 156 (1974).

111. *Id.* at 1016-17. The court noted, however, that the pressures created by preliminary procedures, including the mini-hearing on the merits and the immense expense of complying with discovery orders, have induced defendants to offer large settlements in many cases. *Id.* at 1019. Nevertheless, the court further recognized that "not a single one of these class actions including millions of indiscriminate and unidentifiable members has ever been brought to trial and decided on the merits." *Id.* at 1018-19. See also Handler & Blechman, *supra* note 36, at 628 n.14.

In *Boshes v. General Motors Corp.*, 59 F.R.D. 589 (N.D. Ill. 1973), an automobile purchaser sued General Motors, alleging that the latter overcharged its dealers due to its monopoly power and that the dealers, in turn, passed the overcharge to him and 30 to 40 million other buyers. The court decided that the purchaser could use the pass-on concept offensively, *id.* at 598-99, but denied his motion to maintain the suit as a class action. *Id.* at 602.

112. 58 F.R.D. 481 (S.D.N.Y. 1973).

113. *Id.* at 483-85.

The inherent unmanageability of consumer class actions is minimized when a state, suing on its behalf and for its political subdivisions, seeks to proceed as class representative of similarly-situated consumers within its borders.¹¹⁴ Federal courts can permit states to recover as class representatives for all resident consumers, can require that treble-damages awards be distributed to individuals with specific claims, and should authorize the states to retain any unclaimed portion of the award as general revenues. This was the result in the *Chas. Pfizer* settlement.¹¹⁵

The third mechanism for consumer representation in a treble-damages suit against final product manufacturers is a *parens patriae* action pursuant to the newly-enacted section 4C of the Clayton Act.¹¹⁶ Prior to the enactment of section 4C, the Supreme Court in *Hawaii v. Standard Oil Co.*¹¹⁷ had rejected a *parens patriae* suit to recover treble damages for injury to the state's general economy.¹¹⁸ Now, although a

114. See, e.g., *Illinois v. Bristol-Myers Co.*, 470 F.2d 1276 (D.C. Cir. 1972) (*per curiam*); *In re Antibiotic Antitrust Actions*, 333 F. Supp. 267, 278, 296 (S.D.N.Y. 1971).

115. See 440 F.2d at 1084.

116. 15 U.S.C.A. § 15c(a) (Supp. 1977). Section 4C was created by the Hart-Scott-Rodino Antitrust Improvements Act of 1976, Pub. L. No. 94-435, Title III, § 301, 90 Stat. 1394. This section provides in pertinent part:

(1) Any attorney general of a State may bring a civil action in the name of such State, as *parens patriae* on behalf of natural persons residing in such State, in any district court of the United States having jurisdiction of the defendant, 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 excluded their claims pursuant to subsection (b) (2) of this section, and (ii) any business entity.

(2) The court shall award the State as monetary relief threefold the total damage sustained as described in paragraph (1) of this subsection, and the cost of suit, including a reasonable attorney's fee.

117. 405 U.S. 251 (1972).

118. *Id.* at 253. In *Georgia v. Pennsylvania R.R.*, 324 U.S. 439 (1945), the Supreme Court permitted Georgia to sue as *parens patriae* for injunctive relief under the antitrust laws, *id.* at 446-47, but in *Hawaii* the Court noted that this did not authorize suits to recover damages for injury to the state's general economy. 405 U.S. at 260. For favorable comment on *parens patriae* actions see Oliff, *Parens Patriae Antitrust Actions for Treble Damages*, 14 HARV. J. LEG. 328, 356 (1977); Note, *The Proposed Antitrust Parens Patriae Act: Overdue Antitrust Relief for Ultimate Consumers*, 45 U. CIN. L. REV. 219 (1976). Professor Handler, a critic of collective consumer actions, see Handler, *The Shift*

state may have suffered no injury from an antitrust violation, it may bring a treble-damages suit as *parens patriae* on behalf of its citizens to recover for any injuries sustained by them. The court can direct that recoveries by the state be distributed to specific claimants or retained as general revenues.¹¹⁹

With Congress's statutory approval of some *parens patriae* actions, the remaining obstacle to their effective use is the Supreme Court's rejection in *Illinois Brick* of offensive pass-on theory. *Illinois Brick* diminished the utility not only of *parens patriae* suits but also of other types of consumer actions. Unless consumers have privity with antitrust violators, they will be unable to recover treble damages. Experience and economic theory have demonstrated, however, that when price-fixing occurs at or above the final product level of mass-produced goods, distributors often may hesitate to instigate treble-damages suits. Consequently, a denial of standing to consumers in these situations removes much of the deterrent effect of the treble-damages provision and inadequately balances the policies reflected in the antitrust statutes.

Price-Fixing by Manufacturers of Mass-Produced Goods Below the Level of the Final Product

When price-fixing occurs in the vertical chain of production of mass-produced goods below the level of the final product, standing to sue for treble damages should be granted to the manufacturers of the final product, regardless of privity. This rule also attempts to accommodate practical considerations of antitrust enforcement with general principles of economic theory. It grants standing to the parties who are most likely to be injured and who have the greatest incentive to sue.

When the manufacturers of a minor component of a mass-produced item conspire to fix prices, the resultant injury generally affects consumers only indirectly.¹²⁰ Moreover, to the extent that the overcharge for a component accounts for only a small percentage of the final product's cost, most consumers lack a sufficient interest to file an individual suit. These consumers theoretically could be represented

From Substantive to Procedural Innovations in Antitrust Suits—The Twenty-Third Annual Antitrust Review, 71 COLUM. L. REV. 1, 9-10; Handler, *Twenty-Fourth Annual Antitrust Review*, 72 COLUM. L. REV. 1, 34-42 (1972), recommends that the Department of Justice be empowered to bring a form of *parens patriae* action. See Handler & Blechman, *supra* note 35, at 674-76.

119. See 15 U.S.C.A. § 15c (Supp. 1977).

120. Cf. Handler & Blechman, *supra* note 35, at 636-38. See also Posner, *A Statistical Study of Antitrust Enforcement*, 13 J.L. & ECON. 365, 409 (1970).

either in a class action or in a *parens patriae* suit, as in a situation involving price-fixing at or above the level of the final product. Unlike the latter situation, however, if the violation occurs below the level of the final product, the final product manufacturer would be a more suitable antitrust plaintiff than the ultimate consumers.

Preferring final product manufacturers over ultimate consumers as treble-damages plaintiffs would avoid both the unnecessary complexities of class action litigation and difficult questions of damages distribution. Unlike intermediate manufacturers, final product manufacturers would not be reluctant to sue the antitrust violators. They generally could finance the litigation more easily and would have less fear of disrupting business relations. More importantly, the principles of elasticity suggest that a monopolistic overcharge for a component product often will be passed at least to the manufacturer of the final product.¹²¹ For example, the demand will be inelastic for a component whose cost is a relatively minor part of the cost of the final mass-produced good; virtually all of a monopolistic overcharge by that component's manufacturer will be passed through intermediate purchasers to the final product manufacturer. Thus, deterrence and compensation also are served best by a grant of standing to the final product manufacturer.

An analysis of cases involving these circumstances further demonstrates the preferability of this rule to the privity requirement established in *Illinois Brick*. In *Carnivale Bag Co. v. Slide-Rite Manufacturing Corp.*,¹²² for example, four manufacturers of clothing, plastic bags, and carryalls filed a class action to recover treble damages for injuries resulting from a price-fixing conspiracy among zipper slider manufacturers. The latter group sold sliders to zipper manufacturers which in turn sold zippers to the plaintiffs. Denying the defendant's motion to dismiss, the district court concluded that *Hanover Shoe* prohibited only the defensive use of pass-on theory.¹²³ It also rejected the argument that the plaintiffs lacked standing because they were outside the target area of the defendants' alleged violations.¹²⁴ Thus, the court's decision granted final product manufacturers the opportunity to prove their losses caused by the antitrust violations of component part manufacturers.¹²⁵

121. See text accompanying note 56 *supra*.

122. 395 F. Supp. 287 (S.D.N.Y. 1975).

123. *Id.* at 291.

124. *Id.* at 292-94.

125. *Id.* at 294. An earlier case reaching a different result was *Wolfe v. National Lead Co.*, 225 F.2d 427 (9th Cir.), *cert. denied*, 350 U.S. 915 (1955), in which paint manufacturers sued the manufacturers of titanium pigment, a

A failure to follow the proposed rule could defeat several policies of the antitrust laws. A privity requirement could frustrate the goal of compensation and deterrence. A perfunctory elimination of the privity rule, however, could defeat the goals of defining a manageable legal standard and of avoiding either multiple liability or the unwarranted use of the pass-on defense. The Court of Appeals for the Third Circuit has dealt with the latter problems unsuccessfully. In *Mangano v. American Radiator & Standard Sanitary Corp.*,¹²⁶ a suit was brought to recover damages caused by an antitrust violation resulting in an overcharge of \$10 to \$20 for plumbing fixtures that were used in buildings selling for as much as \$30,000. The vertical chain of production and distribution extended from plumbing fixture manufacturers through wholesalers, plumbing contractors, and general contractors to either the first or, in some instances, the second owners of home, apartment, and commercial buildings. Although the Third Circuit held that *Hanover Shoe* required dismissal as to the owner plaintiffs because of the insuperable burden of proving that the overcharge was passed to them,¹²⁷ it also doubted that the price of a house would be influenced by the small amount of the overcharges.¹²⁸ Nevertheless, the court later affirmed a settlement ap-

component of their paint, for fixing prices and allocating amounts purchaseable by paint manufacturers. Because the defendant's quota system gave preferential treatment to the plaintiff, however, the paint manufacturers could not demonstrate injury. As a result, the Ninth Circuit affirmed the dismissal of the suit. *Id.* at 434. Relying on the *Oil Jobber Cases*, the court's opinion suggested that the plaintiffs must bear the burden of proving not only that the competitive price would have been lower than the fixed price, *id.* at 432-33, but also that they did not pass the overcharge to their customers. *Id.* The plaintiffs failed to meet both burdens. The suggestions presented in this Article, however, indicate that the cases should have been distinguished. In *Wolfe*, the antitrust violation occurred below the level of the final product; standing to sue should have been granted to the final product manufacturer. A presumption that the overcharge was passed-on therefore was inappropriate. In the *Oil Jobber Cases*, the antitrust violators were the final product manufacturers; the courts correctly sustained the defensive use of pass-on theory against the plaintiff wholesalers.

126. 438 F.2d 1187 (3d Cir. 1971), *aff'g per curiam* Philadelphia Hous. Auth. v. American Radiator & Standard Sanitary Corp., 50 F.R.D. 13 (E.D. Pa. 1970).

127. 438 F.2d at 1188. *Cf.* *Balmac, Inc. v. American Metal Products Corp.*, 1972 Trade Cas. ¶ 74,235 (N.D. Cal. 1972) (heating contractors and builder owners denied standing to sue gas vent pipe manufacturers for price fixing; *Hanover Shoe* required privity between plaintiffs and defendants). *But see In re Master Key Antitrust Litigation*, 1973-2 Trade Cas. ¶ 74,680 (D. Conn. 1973), *appeal dismissed*, 1975-2 Trade Cas. ¶ 60,648 (2d Cir. 1975) (states, cities, builder-owners, and private owners who bought hardware indirectly from price-fixing manufacturers had standing to sue: *Hanover Shoe's* rejection of passing-on defense did not extend to its offensive use).

128. 438 F.2d at 1188.

proved by the district court, despite the objection of some contractors that they did not receive adequate damages.¹²⁹ The appellate court rejected the contractors' contention in part because they probably had passed the overcharge to the building owners.¹³⁰ Thus, the court permitted the defendants to use the pass-on concept against both groups of plaintiffs.

In some situations, homes, apartments, and buildings should be characterized as specially constructed and contracted products. Nevertheless, when a tract builder constructs several hundred houses, the buildings are similar to mass-produced products. In *Mangano*, in which some individual claims were quite small, the court was correct in refusing standing to individual home owners.

CONCLUSION

Congress probably will repeal legislatively the absolute privity requirement established by the Court in *Illinois Brick*.¹³¹ A perfunctory reversal, however, would aggravate the problems of multiple liability,

129. *Ace Heating & Plumbing Co. v. Crane Co.*, 453 F.2d 30, 34 (3d Cir. 1971), *aff'd* Philadelphia Hous. Auth. v. American Radiator & Standard Sanitary Corp., 322 F. Supp. 834 (E.D. Pa. 1971).

130. *Id.*

131. Currently, five proposals designed to overrule *Illinois Brick* are under consideration by the Congress. The first bill introduced for this purpose, H.R. 7788, would amend § 4 of the Clayton Act to permit recovery by a purchaser "without regard to whether or not such person was injured as a result of a direct contract or agreement with the defendant." H.R. 7788, 95th Cong., 1st Sess. (1977).

Two proposals, H.R. 8359 and S. 1874, were identical bills introduced in the Senate Subcommittee on Antitrust and Monopoly and the House Subcommittee on Monopolies and Commercial Law by their respective chairmen, Senator Edward M. Kennedy and Representative Peter W. Rodino. These bills would amend § 4 of the Clayton Act to permit a suit by any person who suffered injury "in fact," whether "directly or indirectly." H.R. 8359, 95th Cong., 1st Sess. (1977); S. 1874, 95th Cong., 1st Sess. (1977). See 823 ANTITRUST & TRADE REG. REP. (BNA) A-4. After hearings, a revised draft bill was reported by the Senate subcommittee to the full Senate Committee on the Judiciary without recommendation. This revised draft amends § 4 to permit both offensive and defensive assertions of passing-on regardless of privity. The revision also precludes class actions on behalf of natural persons who have not dealt directly with the defendant, with the exception of state *parens patriae* actions. See 847 ANTITRUST & TRADE REG. REP. (BNA) A-3.

Another proposal, H.R. 10783, was introduced by Representative John F. Seiberling. This bill amends § 4 to read: "Any person including any indirect purchaser . . . may sue . . ." It neither provides for a defensive assertion of passing-on nor limits class actions, but rather permits transfer and consolidation of § 4 suits. H.R. 10783, 95th Cong., 2d Sess. (1978).

damages distribution, and formulation of a manageable legal standard that prompted the Court to grant standing only to those plaintiffs in privity with the antitrust violator.¹³² These problems were far from illusory, and their accommodation with the goals of compensation and deterrence can be achieved only by identifying and preferring the most appropriate antitrust plaintiffs, as in the three situations discussed in this Article. This balancing process is a legislative task that Congress successfully can complete by considering both economic theory and the practical aspects of antitrust enforcement.

132. 431 U.S. at 730, 737-41.