

## Loyola Consumer Law Review

---

Volume 10 | Issue 2

Article 6

---

1998

# Pharmacies Charge Prescription Drugs Manufacturers and Wholesalers with Antitrust Violations Through Price-Fixing Conspiracy

Karina Zabicki

Follow this and additional works at: <http://lawcommons.luc.edu/lclr>

 Part of the [Consumer Protection Law Commons](#)

---

### Recommended Citation

Karina Zabicki *Pharmacies Charge Prescription Drugs Manufacturers and Wholesalers with Antitrust Violations Through Price-Fixing Conspiracy*, 10 Loy. Consumer L. Rev. 130 (1998).

Available at: <http://lawcommons.luc.edu/lclr/vol10/iss2/6>

This Recent Case is brought to you for free and open access by LAW eCommons. It has been accepted for inclusion in Loyola Consumer Law Review by an authorized administrator of LAW eCommons. For more information, please contact [law-library@luc.edu](mailto:law-library@luc.edu).

*Schwartz* are similar insofar as they are both “based upon the assumption that a toxic substance acts immediately upon the body to produce injury,” RSI cases are distinguishable in this respect. The court in the present case held that “the justifications that gave rise to the exposure rule do not apply” in RSI cases because a keyboard is not “an inherently toxic or dangerous substance.” Someone who touches or uses a keyboard is not doomed to contract RSI; rather, RSI results from “an accumulation of events.”

The court weighed several other policy considerations in reaching its final ruling. The court noted a balance between “a defendant’s interest in repose” and “the injured person’s interest in having a reasonable opportunity to assert a claim.” In addressing these two policy objectives, the court noted that there was a possibility of false claims in cases where “excessive

factual inquiries would be necessary.” The court also mentioned the difficulty of tracing the history of latent injuries. A related policy the court considered was that defendants have an extra burden in RSI cases since the history of a latent injury is difficult to trace. The court further recognized the possibility of a “causal break” between a defendant’s alleged negligence and a plaintiff’s claimed injury. Additional considerations included the promotion of justice, stability to human affairs, judicial economy, self-reformation by defendants, and possible unfairness to defendants who might have to defend against stale claims, and questions of credibility and professional diagnostic judgment.

In its final analysis, the court concluded that the cause of action for a keyboard user inflicted by RSI accrues when the user first

experiences symptoms of RSI or when he last used a keyboard, whichever happened earlier. The court noted that RSI cases pose certain problems of proof. The court explained, however, that it had tried to find the “proper balance between giving a plaintiff an opportunity to commence an action after becoming aware of a symptom of injury and providing certainty and predictability to manufacturers, employers and other economic actors in their risk assessment, while also avoiding stale claims.” In sum, the Court of Appeals of New York answered the certified question in the negative, remitted the case to the Supreme Court of New York, and ordered the Supreme Court to rule on RSI cases in accordance with its the ruling.

**CLR**

## Pharmacies Charge Prescription Drugs Manufacturers and Wholesalers with Antitrust Violations Through Price-Fixing Conspiracy

*By Karina Zabicki*

***In re Brand Name Prescription Drugs Antitrust Litigation***, 123 F.3d 599 (7th Cir. 1997), the United States Court of Appeals for the Seventh Circuit reversed the decision of the Northern District Court of Illinois, holding: (1) indirect purchasers may not bring suit against manufacturers in federal court for an overcharge that direct purchasers

allegedly passed on to the indirect purchasers; (2) sufficient evidence existed to create a jury issue of whether the direct purchasers were participants in a price-fixing conspiracy; (3) a suit brought in an Alabama state court claiming a violation of state antitrust laws defeated the application of the “artful pleading” doctrine; and (4) a newly-merged company which

abandoned its predecessor’s participation in the alleged conspiracy did not clear it of liability for its predecessor’s antitrust violations.

This litigation involved hundreds of price-fixing cases brought under Section 1 of the Sherman Act, 15 U.S.C. § 1. Plaintiffs and Defendants appealed four of these rulings, which the Seventh Circuit

consolidated into a single appeal. Retail pharmacies brought suit against manufacturers and wholesalers of prescription drugs, complaining that the wholesalers and manufacturers conspired to deny discounts for brand name drugs to all pharmacies while granting these discounts to favored customers. The pharmacies alleged that Defendants conspired to fix the pharmacies' prices by using a "chargeback system."

### ***Chargeback System Allowed Manufacturers to Give Discounts Below Wholesale Price to Selected Groups***

Under the chargeback system, manufacturers contracted with favored customers, such as hospitals, HMOs, nursing homes, and mail order companies, to set the discounted price at which favored customers could buy prescription drugs from wholesalers. The wholesalers bought the drugs at full price from the manufacturers and later sold the drugs to one of these favored customers. The manufacturers then reimbursed the wholesalers for the difference between the full wholesale price and the discounted wholesale price. Under this system, wholesalers could only give discounts to customers with whom the manufacturers had negotiated a lower price. Additionally, this system prevented the favored customers from engaging in arbitrage, a process in which the favored customers over-ordered drugs in order to create their own surplus which they then resold to pharmacies that were not granted favored customer status.

The favored customers created a

win-win situation for both themselves and the pharmacies when they resold their surplus for a price between the discounted wholesale price and the regular wholesale price. For example, if the regular wholesale price was \$100, the pharmacies would be forced to pay this full amount when buying directly from the wholesalers. However, the favored customer, who paid a discounted wholesale price of, say, \$75, could sell any surplus to the pharmacies for any price between \$75 and \$100 and still realize a profit. As a result, the manufacturers lost money by being underbid by the favored groups who sold their surplus to the pharmacies.

Plaintiffs argued that manufacturers created the chargeback system to employ price discrimination between customers and prevent underbidding. Under the system, the manufacturers would allow wholesalers to give a discount only to those whom the manufacturers had chosen to receive a discount.

### ***Pharmacies Objected to the Effect of Price Discrimination***

Plaintiffs argued that the high prices they paid for the drugs were not the result of individual manufacturers responding to the market forces, but the result of a collusive effort. Plaintiffs produced evidence showing that the manufacturers and the wholesalers agreed among themselves to use the chargeback system to prevent the pharmacies from obtaining discounts. Plaintiffs objected that, but for this alleged conspiracy, the drug prices would fall due to market competition.

In response to this claim, the manufacturers argued that Plaintiffs had not produced sufficient evidence of collusion to justify a trial for a Sherman Act violation and moved for summary judgment. This decision was not appealed. Instead, the district court made four other findings that were appealed.

First, the district court refused to dismiss the pharmacies' "indirect purchaser" claims, which maintained that the pharmacies were overcharged because of Defendants' alleged conspiracy. Manufacturers had moved to dismiss the pharmacies' Sherman Act claim for overcharges by arguing that only parties who purchased drugs directly from the manufacturer, such as wholesalers, could bring such an action. Because the pharmacies were indirect purchasers who did not buy directly from the manufacturers, but rather bought from the wholesalers, they would not have standing to bring an overcharge claim. Second, the district court refused to remand a class action that alleged violation of Alabama's antitrust statute which, contrary to federal law, expressly authorizes suits by indirect purchasers. Third, the district court granted summary judgment to the wholesaler Defendants, concluding there was not enough evidence of collusion with the manufacturers. Finally, the district court granted summary judgment to one of the manufacturers, DuPont Merck Pharmaceutical Company, because DuPont's pharmaceutical division was taken over by DuPont Merck two years after the beginning of the alleged conspiracy, at which time DuPont Merck immediately stopped the discounting practices. The Seventh Circuit discussed each of the four issues separately.

### ***Pharmacies Could Not Sue Manufacturers for Antitrust Violations Because They are Indirect Purchasers***

First, the court addressed whether the district court should have dismissed the indirect purchasers' conspiracy claim. The pharmacies had argued that they should be able to recover damages from the manufacturers for being overcharged by the wholesalers. The pharmacies asserted that the manufacturers were responsible for the pharmacies being overcharged because the chargeback system forced the wholesalers to overcharge non-favored customers. Although wholesalers were reimbursed by the manufacturers for any discount the wholesalers gave to favored customers, wholesalers could not recover the difference between the wholesale drug price and any discount that the wholesalers gave to non-favored customers. The district court had determined that because the wholesalers were nothing more than the manufacturers' "glorified warehouses," or strawmen, the pharmacies were essentially the direct purchasers.

The appellate court turned to case law to address this issue. In *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), the United States Supreme Court held that only direct purchasers, not indirect purchasers, could sue manufacturers for antitrust violations because of the practical difficulty of tracing and apportioning price fixing damages through successive layers of purchasers. The Court recognized one exception to the indirect purchaser rule—when "the direct purchaser is owned or controlled by

its customer." *Illinois Brick*, 431 U.S. at 736 n. 16. The Seventh Circuit also posited another exception to the *Brick* doctrine—when the customer is controlled by the direct purchaser. However, because the wholesalers in the present case were not owned or controlled by the manufacturers, the first exception was inapplicable. This exception did not apply because only the wholesalers themselves could sue the manufacturers for overcharging the wholesalers. Therefore, the Seventh Circuit reversed the district court and held that the pharmacies' indirect purchaser overcharge claims against the manufacturers should have been dismissed.

### ***State Class Action Suit Removed to Federal Court Should be Remanded to State Court***

The second issue the court considered involved a class action suit that claimed to be based on an Alabama statute modeled after the Sherman Act, which was filed on behalf of consumers in several states. There was a crucial difference between these state and federal statutes because the state statute authorized indirect-purchaser claims, whereas the federal statute barred claims by indirect purchasers under *Illinois Brick*. Because *Illinois Brick* favored Defendants, they had removed the case from state court to federal court. Plaintiffs, on the other hand, wanted the case remanded, but the district court denied their request to remand and Plaintiffs subsequently appealed.

A federal court has jurisdiction over cases involving party diversity

or federal questions. In reviewing removal based on diversity, the appellate court found complete diversity between the parties but found that Defendants could not show that Plaintiffs met the statutory minimum amount of \$50,000 damages in a diversity action. Because Defendants introduced no evidence that any of the named Plaintiffs individually met, or could have met this statutory minimum, Defendants needed another way to meet the requirement. Because Plaintiffs were also seeking injunctive relief, the minimum statutory amount could have been met if Defendants could prove that the injunction imposed a cost of compliance in excess of \$50,000.

The court specified four ways in which Defendants could establish that an injunction would meet the statutory minimum. These included: (1) the anticipated value to the Plaintiffs of granting the injunction would exceed the required minimum amount; (2) the injunction would cause Defendants to change a way of doing business which would cost the statutory minimum amount; (3) by complying with the injunction, defendants would have to sacrifice some benefit worth more than the minimum amount in controversy; or (4) the ministerial or clerical costs resulting from compliance by Defendants might carry a case across the threshold. The only one of these four alternatives that Defendants attempted to prove was the fourth option regarding clerical costs. The court held that because Defendants failed to produce evidence quantifying the cost of compliance, Defendants could not prove that the federal court had appropriate jurisdiction.

The district court had also allowed the removal of the state suit to the federal court based on another jurisdictional theory called the "artful pleading" doctrine, which the appellate court proceeded to analyze. The doctrine usually applies in a situation where federal law has preempted an area of dispute so as to make state law an inappropriate source for a remedy to resolve the dispute. "Artful pleading" describes a plaintiff's often underhanded attempt to artfully cast "essentially federal law claims as state law claims," perhaps by evading reference to any federal law. Using artful pleading, a plaintiff would attempt to keep his or her claim in state court to avoid certain consequences unique to federal courts applying federal law. Courts use the doctrine to ferret out plaintiffs who bring state law claims in an effort to circumvent federal law where federal law has dominated the area of dispute. Therefore courts, like the district court in this case, allow removal of a state law claim to federal court even though diversity or a federal question may be lacking.

The appellate court disagreed with the district court's assessment of the artful pleading doctrine. The court reasoned that although Plaintiff's only motive for filing a claim under a state statute was to circumvent the *Illinois Brick* doctrine, invoking the artful pleading doctrine would have been proper only if the Plaintiffs had no other possible relief in state court. However, the appellate court explained that there was a means of relief, however tenuous, in filing the case in state court by invoking Alabama antitrust law. In its analysis, the court found that the Alabama antitrust statute may apply

to the case at bar even though it involved Plaintiffs from more than one state. Defendant wholesalers argued that Alabama's antitrust statute was limited to intrastate commerce; therefore, Plaintiffs had to invoke federal antitrust laws. The court agreed that if the present case had challenged sales from other states to pharmacies outside of Alabama, an example of pure interstate commerce, then Alabama law would not apply because a state could not have regulated sales that took place wholly outside it. However, because the present case challenged sales from other states to pharmacies in Alabama, the court found that this type of suit fell into the permissible scope of the Alabama antitrust statute. The court held that the case could defeat the artful pleading doctrine because it had merit, and the district court erred in denying the motion to remand the suit to the Alabama state court.

### ***Enough Evidence Existed Against Wholesalers to Preclude Their Dismissal from Suit***

The next issue the Seventh Circuit examined was whether Plaintiffs produced enough evidence to establish a jury issue of whether the wholesalers were part of a price-fixing conspiracy. The wholesaler Defendants claimed that "it would have been contrary to their economic self interest for them to have joined a conspiracy that prevent[ed] them from selling at a discounted price to pharmacies." However, pretrial discovery demonstrated that wholesalers had incentives to commit to the conspiracy, namely, to make sure

the wholesalers were not pushed out as middlemen by the manufacturers dealing directly with customers. The court reversed the district court and held that regardless of whether Plaintiffs' theory was true, there was enough evidence to defeat a motion for summary judgment.

### ***DuPont Merck Obligated to Pay for Sins of its Predecessor***

Finally, the court determined whether the district court properly carved out DuPont Merck from Plaintiffs' claims of a conspiracy. DuPont Merck was formed as a result of the joint venture between DuPont and Merck, which took place two years after the alleged conspiracy began. The new venture abandoned participation in the chargeback system as soon as it was formed. Based on this fact, DuPont Merck argued that it had cut its ties with the manufacturers who participated in the alleged conspiracy and thus was not properly joined as a defendant. The appellate court disagreed. It held that there was enough contrary evidence to preclude summary judgment in DuPont's favor. DuPont Merck was liable for the company's antitrust violations prior to the merger because it had not adequately cut its ties to those still involved with the conspiracy. The court reasoned it was not enough to merely change policies and cease involvement to adequately withdraw from a conspiracy. Rather, to guard against liability, a company's withdrawal must have been accompanied by either disclosure of the conspiracy to the authorities or an announcement of the withdrawal to any coconspirators. Because it

appeared that DuPont Merck silently withdrew, the court found it was not free from the ramifications of the alleged conspiracy. Therefore, the court reversed the district court and held that DuPont Merck had been improperly dismissed.

In conclusion, the Seventh

Circuit reversed the four rulings of the district court, which Plaintiffs appealed from by holding that: (1) indirect purchasers were barred from filing suit against manufacturers under federal law; (2) the class action suit filed pursuant to Alabama antitrust law

should have been remanded to state court; (3) the wholesalers were improperly dropped as defendants; and (4) DuPont Merck was improperly dismissed as a defendant.

**CLR**

## California Judicial Candidate Requirements Did Not Violate the U.S. Constitution

By Sara Marzullo

In *NAACP v. Jones*, 131 F.3d 1317 (9th Cir. 1997), the United States Court of Appeals for the Ninth Circuit held that Los Angeles County's (the "County") reimbursement system (the "system"), which requires judicial candidates to reimburse the County for printing their candidate statements in the Official Sample Ballot and Voter Information Booklet and which does not provide public funding for campaigns, does not violate the Equal Protection Clause of the Fourteenth Amendment or any fundamental right under the First Amendment.

Each judicial candidate may print a 200-word statement in the Official Sample Ballot which is circulated to every voter in the County that describes his or her background and position on the issues. Under a practice known as the "cost-reimbursement requirement," however, all judicial candidates may be required to reimburse the County for the printing costs of their statements in the Official Sample Ballot and Voter

Information Booklet. By statute, the County Board of Supervisors can decide each campaign year whether judicial candidates will have to reimburse the County for the costs of printing. See CAL. ELEC. CODE § 13307 (West 1997). When the Supervisors require these cost-reimbursement payments, these payments do not fund elections, and the County may not retain them.

In response to the cost-reimbursement requirement, the NAACP, Charles Lindner (a former candidate), and voters of the County ("Plaintiffs") brought suit against the Secretary of State of California, Bill Jones, and other County officials ("Defendants"). Plaintiffs alleged that the County's campaign rules created a "wealth primary" forcing candidates to spend a significant amount of money to run a meaningful campaign.

Plaintiffs argued that the "wealth primary" violated the First Amendment and the Equal Protection Clause of the Fourteenth Amendment, and they sought declaratory and injunctive relief.

Plaintiffs contended that the County should print every candidate's statement free of charge and create a public fund for potential candidates that would allow them to run meaningful campaigns.

The district court dismissed Plaintiffs' claims against Secretary of State Jones pursuant to Fed. R. Civ. P. 12(b)(6) for failure to plead with specificity. In particular, Plaintiffs failed to plead specific incidents showing Jones violated their rights. In addition, the district court dismissed Plaintiffs' claims against the other Defendants for lack of standing because they failed to allege an "injury in fact." Plaintiffs also brought state law claims but did not appeal them.

### ***No "Heightened Scrutiny" Applied***

On appeal, the Ninth Circuit first determined whether it should analyze Plaintiff's equal protection claim by using a "heightened scrutiny analysis." Courts apply a