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The Law and Economics of (Functional) Antitrust Standing in the United States and the European Union

Jeffrey L. Harrison
University of Florida Levin College of Law, harrisonj@law.ufl.edu

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I. INTRODUCTION

Aside from interpretations of the substantive law, the level of private antitrust enforcement in both the United States and the European Union is a function of a number of factors. The most important of these are: (1) The availability of punitive or exemplary damages; (2) The possibility of recovering attorney's fees; (3) The difficulty of creating a class of plaintiffs or of obtaining collective redress; (4) The ease of discovery; and (5) Definitions of what qualifies one to bring a private action. This discussion is about the last of these—eligibility or, in the language of U.S. antitrust law, standing.[1] Eligibility or antitrust standing alone, however, is a relatively empty notion as far as having an impact on the actual level of private actions.[2] Consequently the focus here is more

* Stephen C. O'Connell Professor of law. University of Florida College of Law.

1. Standing, as will be discussed below, means one is eligible to bring an antitrust action. As a general matter it means one has been directly affected by the alleged violation of the antitrust laws.

2. The rationale for this is easy to understand. An eligible plaintiff who has only a 50% chance of prevailing and who may only recover single damages and no punitive damages may

operational and adopts the concept of "functional standing." More specifically: What is the likelihood that private enforcement will be a significant force with respect to antitrust enforcement? Functional standing is dependent upon standing in the formal sense—a procedural component—and expected or likely damages—a substantive component.

To date, and despite pressures toward convergence,[3] the United States and the European Union have taken different paths with respect to the enforcement of antitrust laws by private parties and, therefore, differ dramatically in levels of functional standing. U.S. law is more encouraging to private enforcement than E.U. law but has a narrower view of whom those private parties are permitted to be.[4] In the European Union, the eligible parties are broad but the motivation of any single party to bring an action is quite low.

In the United States, the substantive law and much of the procedural law flow from federal courts' interpretations of the Sherman Act[5] and the Clayton Act.[6] Because this is all federal law, general statements are more appropriate. In the European Union, the substantive antitrust provisions are those found in the Treaty on the Functioning of the European Union.[7] Procedural requirements as they pertain to private actions are determined by national courts.[8] Consequently, any general statements about the eligibility or standing are more problematic. Indeed, one of the issues faced by the European Union is achieving

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not find ligation attractive. The fact that standing exists in a technical sense is, therefore, irrelevant.

3. *See generally* Kfir Abutbul, *The U.S. and E.U. Approaches to Competition Law - Convergent or Divergent Paths?* 17 COLUM. J. EUR. L. 103 (2010). The most recent indication of convergence is a July 11, 2013 Proposal for a Directive of the European Parliament and of the Council [hereinafter "Proposal"]. That proposal was adopted by the Council of the European Union and the European Parliament in December 2013. It requires approval by the European Parliament and the European Commission after which member states would be given two years to adopt the contained proposals. Those proposals would make private actions far more likely. *See Proposal for a Directive on Antitrust Damages Actions*, http://ec.europa.eu/competition/antitrust/actionsdamages/proposed_directive_en.html (last visited, Jan. 15, 2014).

4. In light of current events national policy could change but at this point those changes are at best years away. Francesco Rizzuto, *The Private Enforcement of European Competition Law, What Next?*, 2010 GLOBAL COMPETITION LITIGATION REV. 57 (2010); Marc A. Sittenreich, *The Rocky Path for Public Directors General: Procedure, Politics, and the Uncertain Future of EU Damages Actions*, 78 FORDHAM L. REV. 2703 (2010); *see also* Assimakis P. Komninos, *Relationship Between Public and Private Enforcement: quod Dei Deo, quod Caesari*, http://papers.ssrn.com/sol3/papers.cfm?abstract_id= 1870723 (last visited Feb. 2. 2014).

5. 15 U.S.C. § 15.

6. *Id.* Individual states may have their own antitrust provisions but these may not conflict with federal law.

7. 55 Official Journal of the European Union, L235 (Sept. 1, 2012).

8. Francis G. Jacobs, *Civil Enforcement of EEC Antitrust Law*, 82 MICH. L. REV. 1364, 1367–68 (1984).

some uniformity with respect to eligibility issues. Nevertheless, as a general matter, there seems to be little question that Europe as a whole is struggling with the eligibility question and whether private enforcement is destined to be a significant factor. Official statements favor greater private enforcement,[9] but the actual incentives for bringing private actions are not compelling.[10] In fact, efforts in the European Union to make compensation broadly available seem destined to have little impact.

Part II sets out the basic legal analysis of "functional eligibility" in the United States and the European Union. Private enforcement, however, is only relevant with respect to specific goals. In antitrust, those goals are compensation and deterrence. Thus the question is: How do two different approaches to functional standing advance two goals that themselves are not always consistent? The purpose of Part II is to describe the two models sufficiently to then apply them to different standard antitrust violations. It concludes the E.U. system, as currently constructed and likely to exist in the future, does not have and will not have a private regime of enforcement that advances either goal. In Part III, this is illustrated in the context of specific economic models.

Two important qualifying notes are in order. First, this offering is about private enforcement only. In both the United States and the European Union, the overall impact of enforcement efforts will be determined by both public and private actions. Weak private enforcement can be offset by strong public enforcement and this applies to both the compensation and deterrence goals.[11] Second, the discussion also does not consider the varying impacts of different policies in individual E.U. member states. The impact of efforts to expand functional standing in any member state will be affected by the availability of collective redress in that state and punitive damages.

II. THE ELIGIBILITY QUESTION

As a matter of theory, the possibility of private enforcement exists along a continuum ranging from very likely to nonexistent. For example, a set of antitrust laws could be enacted that involve no public enforcement at all but which allow anyone—whether affected or not—to file an action and collect punitive or statutory damages. This might be

9. SIMON VANDE WALLE, PRIVATE ANTITRUST LITIGATION IN THE EUROPEAN UNION AND JAPAN 162–63 (2013).

10. In effect, increased eligibility without the promise of punitive damages may mean that private enforcement is no more likely.

11. A strong deterrence function alleviates the need for compensation by preventing harm in the first place.

called the pure "bounty hunter" model. Between the bounty hunter model and one in which there is no private enforcement there are a number—perhaps an infinite number—of positions. The position chosen is ultimately a matter of policy and can be compared to turning on or off a private enforcement faucet. This faucet can be adjusted in a number of ways but, for purposes of this article, the faucet is controlled by the breadth of functional standing which is in itself dependent on both eligibility and financial incentives. One without the other means little or no private enforcement.

On first impression the choice of how to proceed with respect to eligibility seems to turn on whether the goal of antitrust law is to compensate victims or to deter anticompetitive conduct before the damages occur. A regime of antitrust law designed to compensate those harmed may look quite different from one designed to punish and deter anticompetitive actions. In the latter case, private actions would have to be readily available. At the most basic level, the question in this respect is closely related to the difference between a civil action based on a tort theory and the enforcement of criminal law. In the tort example, the objective is simply to restore the party damaged to a "but for" position.[12] In fact, those measures may still mean anticompetitive action has a net positive outcome for those involved. Put differently, if the only goal is compensation, then from the firm's point of view, it may be profit maximizing to harm others as long as the revenues generated exceed the cost of compensation.[13]

In the deterrent or criminal law model, the objective is to prevent the damage from occurring.[14] This objective is achieved by going further than requiring the offending party to pay damages or to disgorge any ill-gotten gains. Punitive sanctions are typically designed to eliminate the profitability of anticompetitive conduct. These punitive sanctions can be implemented by fines, imprisonment, or awarding supra compensatory damages. One need not compensate victims in order to deter anticompetitive conduct.

The distinction between compensation and deterrence is, however, more theoretical than real. Anticompetitive conduct generates externalities in the form of higher prices, lower output, and reduced

12. This assumes the absence of punitive damages. Although a highly artificial notion, the idea is to compensate the individual so that he or she would be indifferent between suffering the harm and being compensated and not suffering the harm at all.

13. Those familiar with contract law will recognize this as analogous to the "efficient breach." In effect, the profit from a violation may exceed the damages to those harmed by the violation. In addition, unless the expected recovery is 100 percent, the expected damages to be paid by the offending party will be consistently less than the actual harm caused.

14. It does this by making the expected loss in litigation exceed the expected gains.

consumer surplus.[15] Compensation offsets that harm, when, and if, all victims are assured of full compensation. Thus, the tort-like regime does restore victims who prevail in a sometimes risky private action. On the other hand, the deterrence model achieves the same end by ensuring that the externality does not occur in the first place. There is no need for restoration if the harm does not occur. In short, antitrust violations are penalized not because of a widespread belief that they are morally reprehensible but because deterrence is a more effective way to address the compensation problem. Moreover, if the only goal is prevention, the eligibility issue is beside the point—any measure that makes anticompetitive behavior unprofitable will achieve that end. Of course, the idea that the deterrence model could ever advance to the point of eliminating any need for *ex post* compensation is fanciful for it would mean there are no violations and, thus, no enforcement actions at all.[16]

Nevertheless, a regime that appears to be strictly deterrence oriented may actually have a powerful compensatory effect. On the other hand, one that is compensation oriented may, subject to the availability of public sanctions, have a very limited deterrent effect. In the next parts, the two systems are examined to determine which model they fit.

A. *The United States*

In the United States, deterrence is favored over compensation but compensation remains an important objective. This is a result of the combined effect of three doctrines—antitrust injury, antitrust standing, and the availability of treble damages.[17] An antitrust injury is the type of injury the antitrust laws are designed to prevent. This limitation results from the statutory requirement that damages only be awarded to those injured "by reason" of activities forbidden by the antitrust laws.[18] The seminal case is *Brunswick Corp. v. Pueblo Bowl-O-Mat.*[19] In that case the plaintiff, an operator of bowling alleys, challenged the acquisition of a competing but failing bowling alley by an upstream supplier arguing that it was an unlawful merger.

The Supreme Court, in ruling that the plaintiff had not suffered antitrust injury, did not address the merits of the claim. Instead, the

15. Consumer surplus is a measure of the benefit to the consumer of buying an item. It is the difference between the amount paid and the most the consumer would be willing to play. For a market, the total consumer surplus is the sum of the consumer surpluses associated with all sales.

16. Any public enforcement action automatically means that there has been harm and, thus, the need for compensation.

17. *See generally* E. Thomas Sullivan & Jeffrey L. Harrison, UNDERSTANDING ANTITRUST AND ITS ECONOMIC IMPLICATIONS 49–68 (6th ed. 2014).

18. The language is from Section 4 of the Clayton Act. 15 U.S.C. § 15.

19. Brunswick Corp. v. Pueblo Bowl-O-Mat, 429 U.S. 477, 488 (1977).

plaintiff was ruled, in effect, "ineligible."[20] The plaintiff's goal in invoking the antitrust laws was to advance its desire to gain market power. The harm from the merger—the inability of the plaintiff to become a monopolist itself—was not "antitrust injury." This is not to say the merger would not ultimately be anticompetitive. That question was not addressed. Instead, the plaintiff's injury was not linked to the possibility of a less competitive market. The antitrust injury requirement is one way in which U.S. law deviates significantly from the pure "bounty hunter" model.[21]

The second requirement—standing—is that the plaintiff must not be too remotely affected by the anticompetitive act.[22] While the injury requirement can be viewed as a straight-forward interpretation of the "by reason of" language of the relevant legislation, the standing requirement is a bit more nebulous and probably more clearly reflects judicial philosophy with respect to the proper level of private antitrust enforcement and its purpose. The standard has been interpreted to mean that an eligible plaintiff must be an efficient enforcer of the antitrust laws. What this means precisely cannot be determined. Important elements include how directly the impact is felt and the likelihood that the plaintiff or plaintiffs are in the best position to advance the procompetitive goals of the antitrust laws.[23] For example, a buyer or seller may have suffered antitrust injury but only as a result of an action that took place several layers above or below the victim in the chain of distribution. That party may have suffered relatively small damages and it would be quite challenging to establish what the actual measure of damages is. This plaintiff would not be viewed as the best private party to advance the goals of the antitrust laws.

The doctrines of antitrust injury and standing developed independently and in a common law like fashion. They have both been revisited and refined over the last four decades.[24] Today, it is accurate to say that in order to have antitrust standing one must have suffered an antitrust injury. Conversely, not all those suffering antitrust injury have antitrust standing. It is important to note a third standard that influences the eligibility issue in certain cases. It fits most logically under the concept of antitrust standing but, because of the sequence in which the U.S. Supreme Court decided the relevant cases, it was not officially

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20. *Id.* at 489.

21. The bounty hunter model would be one that brought any violator of the antitrust laws "to justice" regardless of the impact on that party.

22. *See* Sullivan & Harrison, *supra* note 17, at 53–55.

23. *See* Associated Gen. Contractors v. Calif. State Council of Carpenters, 459 U.S. 519, 541–42 (1983).

24. *See* Roger D. Blair & Jeffrey L. Harrison, *Reexamining the Role of Illinois Brick in Modern Antitrust Standing Analysis*, 68 GEO. WASH. L. REV. 1 (1999).

viewed as a standing decision. The issue involves the eligibility of those who purchase from those who have paid supracompetitive prices due to collusion of their suppliers. Specifically, if a firm buys from another firm that itself buys from upstream firms that are price fixing, can that indirect purchaser collect damages based on the amount of the overcharge[25] that is passed through by the firm from which it purchased? The U.S. Supreme Court, in *Illinois Brick Co. v. Illinois*,[26] answered that indirect purchasers may not recover. As already noted, the decision was made before modern injury and standing doctrines became focused. A more modern interpretation of the policy is that indirect purchasers from price fixing firms have suffered antitrust injury but ultimately do not have standing.

The direct/indirect purchaser standards, like standing more generally, do not necessarily flow from the U.S. antitrust statutes but reflect judicial efforts to answer questions left open by that legislation. Although these doctrines are relatively well developed in U.S. antitrust law, there are important nuances that should not be missed. First, the fact that a party may lack standing or may not have suffered an antitrust injury does not involve the question of whether there has been a substantive violation of the antitrust laws. For example, as already noted, in the leading antitrust injury case, *Brunswick Corp. v. Pueblo Bowl-O-Mat*,[27] the Court did not reach the issue of whether anticompetitive actions had occurred. Instead, in an injury inquiry, a court examines the plaintiff's theory of how it was injured individually and if that injury is the type the antitrust laws are designed to avoid. If not, the inquiry stops. A ruling that a party does not have standing creates the risk of an under-enforcement error. A ruling that a party does have standing does not, however, create the risk of over-enforcement since that party must still demonstrate a substantive violation.

A final element that complements the ideas of standing and antitrust injury is the availability of treble damages.[28] In effect, plaintiffs demonstrating damages recover that amount multiplied by three. The importance of this can be understood by noting the simple cost/benefit analysis of the decision to pursue an antitrust action. The probability of prevailing in any antitrust action is less than 100%. This means that if the only damages recoverable are equal to the actual harm the expected recovery is always less that the amount of harm. More importantly, the expected loss to the defendant will also be less that the harm caused. A regime of single damages discourages private enforcement efforts and

25. The overcharge is the difference between the price charged by the price fixing firms and that charged in the absence of price fixing.

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

27. Brunswick Corp. v. Pueblo Bowl-O-Mat, 429 U.S. 488 (1977).

28. 15 U.S.C. § 15.

increases the profitability of engaging in anticompetitive activities.

When all of these factors are combined, the U.S. system is more deterrence centered than compensation centered. This is principally a consequence of a relatively narrow standard with regard to standing particularly in the form of excluding indirect purchasers. A focus on compensation, as noted earlier, is one that attempts to return those harmed to the ex-ante *status quo*. In its fullest form, it requires tracing the impact of the anticompetitive harm through layers of buyers and sellers. For example, a horizontal agreement on the price of a raw material may have an impact on manufacturers of a product, as well as its wholesalers, retailers and final customers. More importantly it would require that defendants be allowed to employ a pass on defense. If this were not the case, there would be overcompensation. On the other hand, a focus on deterrence means that it is important to have at least one highly motivated plaintiff who has much to gain from a successful action whether or not that gain is equal to the actual loss suffered. This means disallowing a pass on defense and adding a punitive element. It is important to note, however, that there is no empirical reason to believe that deterrence means compensation goals are not largely met in the sense that the harms to be compensated do not occur in the first place.

An excellent example of how the deterrence and compensation policies interact is *Illinois Brick*.[29] A compensation function would have likely meant allowing indirect purchasers to recover. This too could potentially reduce the damages paid since the impact as one goes the through the chain of distribution likely decreases along with the ease of demonstrating the amount of actual loss. A policy of no indirect action, when coupled with the disallowance of a pass on defense means one set of directly affected plaintiffs will have the maximum incentive to bring an action. This is not entirely inconsistent with compensation but it relegates compensation to a secondary concern. On the other hand, exposure to treble damages may mean aggressive private action by those directly affected and, in a sense, protect downstream purchasers from harm.

B. *The European Union*

A comparison of the U.S. and E.U. standards with respect to injury, standing, and damages cannot be a straightforward one in part because private enforcement in the European Union is still relatively infrequent and the doctrines are considerably less stable than in the United States.[30]

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29. *Illinois Brick Co.*, 431 U.S. at 720.

30. *See generally* Sittenreich, *supra* note 4; Ingrid Gubbay & David Romain, *Plaintiff Recovery Actions*, EUR. ANTITRUST REV. (2011); David Romain & Ingrid Gubbay, *Competition Claims: Uneven Progress, Still*, 2001 EUR. ANTITRUST REV. 47; John Pheasant, *Damages*

Private antitrust actions must be brought in national courts. The issues of standing and injury are generally regarded as procedural, and each national court's procedural rules govern. These rules often differ from nation to nation.[31] In addition, the distinction between standing and "functional standing" is especially important. Even the most liberal notions of standing do not translate into functional standing if financial incentives are absent. This means the regimes could be very much alike with respect to standing and injury but overall be very different with respect to private enforcement generally.

A good place to start in attempting to understand the lack of clarity and the limitations in the European Union with respect to private actions is *Courage v. Crehan*,[32] the case most responsible for initiating greater interest in private actions. The court in that case wrote that enforcement "must be open to any individual to claim damages for loss caused to him by a contract or by conduct liable to restrict or distort competition."[33] The "any individual" wording strongly suggests a broad notion of standing and "caused to him" is consistent with a compensation goal. That theme is reflected in the 2008 White Paper[34] which includes a number of specific proposals designed to facilitate an increase in private actions. The White Paper clearly focuses on "compensation" as the primary goal of private actions.[35] Thus, plaintiffs should "receive full compensation of the *real value* of the loss suffered."[36] In addition, "[f]ull compensation is the . . . first and foremost guiding principle."[37] The drafters of the White Paper do observe that greater compensation will mean a greater level of deterrence but any real effort to include a deterrence element to private enforcement is undercut by a continued reluctance to allow for punitive damages or contingent fee arrangements. Interestingly, the White Paper deviated from the Green Paper[38] created three years earlier, by dropping

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Actions for Breach of Antitrust Rules: The European Commission's Green Paper, 27 EUR. COMPETITION L. REV. 367 (2006); Thomas Rouhette, *The Availability of Punitive Damages in Europe: A Growing Trend or a Non Existent Concept*, 74 DEF. COUNSEL J. 320 (2007).

31. Christopher J. Cook, *Private Enforcement of E.U. Competition Law in Member State Courts: Experience to Date and Path Ahead*, 4 COMPETITION POL'Y INT'L 3 (2008).

32. Case C-453-/99, Courage v. Crehan [2001] ECR I-6297.

33. European Commission 2008, White Paper on Damage Claims for Breach of EC Antitrust Rules, COM 165 final [hereinafter White Paper]. *See generally* Tim Reher, *The Commission's White Paper on Damages Actions for Breach of the EC Antitrust Rules*, 2009 EUR. ANTITRUST REV. 38 (2009).

34. White Paper, *supra* note 33, at 2.

35. *Id.* at 7 (emphasis added).

36. *Id.* at 3.

37. *Id.*

38. European Commission 2005, Green Paper on Damages for Breach of the EC Antitrust Rules, COM 672 final [hereinafter Green Paper].

a proposal for punitive damages. In effect, the European Union opts to rely on public enforcement as the principal deterrence instrument[39] and, as noted earlier, this can have what might be viewed as an *ex ante* compensation effect.[40] Whether this is a realistic expectation is another matter. Nevertheless, when compared to the United States, the European Union has opted to use private actions almost exclusively for compensation.

One of the stickier issues that falls within the discussion of compensation and deterrence is the availability of a pass on defense. The 2006 Green Paper suggests a variety of options for dealing with the direct/indirect purchaser problem, including both allowing and not allowing the pass on defense.[41] The more recent White Paper is more specific and proposes that defendants (infringers) be permitted to apply a "passing on" defense[42] and plaintiffs may make offensive use of the pass on theory. It is important to remember, though, that these statements do not ensure compliance by national courts. Nevertheless, in theory, a fully developed compensation approach would mean that defendants who were able to show that plaintiffs had passed overcharges onto downstream purchasers[43] would be able to deduct those amounts from an award. Otherwise, there would be overcompensation. The impact of this deviation from U.S. policy is to increase the compensation goal of private actions while decreasing the deterrence goal. Indeed, one of the arguments for compensation over deterrence is the express desire not to become like the United States.[44] All of these themes are found in the more recent 2013 Proposal[45] which does increase the possibility of national uniformity but still lacks the critical element of providing a significant financial incentive.

One interesting lack of clarity is raised by the decision in *Courage* and relates to the notion of antitrust injury. A literal interpretation of the wording in *Courage* allows an action by someone injured as the result of a market "distortion." Whether "distortion" is the same as movement from more competitive to less competitive conditions is not clear. Veljko Milutinovic offers the example of a situation in which small competitors collude to compete more effectively against a dominant

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39. *See* Sittenreich, *supra* note 4; Woulter P.J Wils, *The Relationship Between Public Antitrust Enforcement and Private Actions for Damages*, 32 WORLD COMPETITION 2 (2009).

40. *See supra* text accompanying notes 16–18.

41. Green Paper, *supra* note 38.

42. White Paper, *supra* note 33.

43 In addition, if downstream purchasers were permitted to act as plaintiffs, the amount of overcharge they passed on would be deductible.

44. VELJKO MILUTINOVIC, THE "RIGHT TO DAMAGES" UNDER E.U. COMPETITION LAW (Amsterdam, Netherlands: Wolters Kluwer 2010).

45. *See* "Proposal," *supra* note 3.

firm.[46] Suppose the dominant firm then brings a private action against the colluding firms. In the United States there would be antitrust injury questions, if not a clear resolution, because the goal of the dominant firm would be to use the antitrust laws to decrease competition. In the European Union, however, the dominant firm may be viewed as having suffered antitrust injury as a result of a market distortion. At least at this point, there is no legislative authority like that in the United States that would further define the kind of injury that must be suffered before the antitrust laws can be invoked.

There can be little doubt that at the highest levels, E.U. officials and agencies intend to increase private antitrust actions. Recent discussions, however, suggest this urging has not been successful as an overall matter.[47] Moreover, it appears that any thought that private antitrust actions will increase substantially is optimistic. Private actions are risky especially in the absence of contingent fees and punitive damages.[48] Added to this are indications that increased standing for private parties will be accompanied by a pass on defense and the offensive use of the pass on rationale.

C. *A Comparison*

Although E.U. and U.S. policies with respect to standing, injury, and indirect purchases can be viewed at different stages of development, there are probably more important policy considerations at work. These policy considerations result in a nearly opposite approach to private actions. In the United States at one level, private enforcement has been designed to be deterrent-oriented and to encourage private actions. Yet, at the same time, the impact of court decisions has been to make the system far less open to plaintiffs. It does not appear to be by accident that at the same time the U.S. Supreme Court was decreasing the scope

46. MILUTINOVOC, *supra* note 44, at 232–33.

47. *See* Rizzuto, *supra* note 4; Gubbay & Romain, *supra* note 30. This may be changing with the 2013 release of the Proposal for a Directive of the European Parliament and of the Counsel, but this is far from obvious. *See* Valentine Mercea, "The Private Enforcement of Competition Rules in the E.U. – A New Starting Line?" Competition Policy International, https://www.competitionpolicyinternational.com/assets/Uploads/EUAugust.pdf (last visited, Jan. 28. 2014); Daniele Calisti & Luke Haasbeek, *The Proposal for a Directive on Antitrust Damages Actions: The European Commission Sets the Stage for Private Enforcement in the European Union*, COMPETITION POL'Y INT'L, Aug. 12, 2013, https://www.competitionpolicyinternational. com/the-proposal-for-a-directive-on-antitrust-damages-actions-the-european-commission-sets-th e-stage-for-private-enforcement-in-the-european-union/ (last visited Jan. 28, 2014).

48. *See* Tim Reher, *The Commission's White Paper on Damages Actions for Breach of the EC Antitrust Rules*, 2009 EUROPEAN ANTITRUST REV. 38 (2009); Monique Hazelhorst, *Private Enforcement of E.U. Competition Law: Why Punitive Damages are a Step Too Far*, 2010 ECONOMIC REV. OF PRIVATE LAW 757 (2010).

of the substantive reach of the U.S. antitrust laws in order to focus on economic efficiency and consumer welfare, it was also narrowing the range of possible plaintiffs.[49] Considered together, the effect of these two changes was to decrease the likelihood of so-called false positive—practices incorrectly labeled as anticompetitive. Nevertheless, there are powerful incentives for private parties to bring antitrust actions in the United States and these incentives further the compensation function as well.

In the United States, defendants may not subtract from the overcharge amounts passed on to the customers of the plaintiff. In all likelihood this means overcompensation for direct purchases but also means a significant deviation from a compensation model since indirect purchasers may not recover for overcharges passed on. It is also worth noting that indirect purchasers to whom the overcharge is passed on may themselves be sellers. If they raise prices and therefore sell less the consequence is a loss in profits. This decline in profit is also not recoverable.

In the European Union, a far different dynamic is in play. There seems to be a general desire to rely on public enforcement as a source of deterrence. If deterrence is sufficiently high, compensation becomes a secondary problem. Nevertheless the policy trend, if not the reality, has been to increase the availability of compensation to private parties. Because damages are limited to single damages, this movement, if successful will have little impact on deterrence since, if left to private actions alone, the net effect of anticompetitive activities may be profit maximizing for firms engaged in those activities. Paradoxically, the increase in the availability of private actions may not increase "functional standing" or have the desired impact on compensation.

III. ECONOMIC MODELS[50]

Basic economic models illustrate that the antitrust remedies available in the United States are not compensatory and they also illustrate what would be compensatory. Compensation, though, is at best an ideal. As explained here, even a moderately comprehensive effort to compensate in the absence of punitive damages and the ability to aggregate claims is likely to fail. The three models below are explained in the text with a more formal presentation found in the margins.

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49. *See* Sullivan & Harrison, *supra* note 17, at 240–45.

50. Much of the following can be understood without a complete understanding of the economic models. Readers should be able to follow the logic.

A. *Model 1: Price Fixing and Consumers*

In Model 1, price fixing firms are selling to consumers. The important feature of this model is that buyers do not resell. U.S. law allows a recovery for "three-fold" the damages suffered. In the typical price fixing case this means three times the overcharge[51] per unit multiplied by the number of units purchased during the period of price fixing.[52] It is important to note that the ability to raise prices must be accompanied by a decrease in output or supply. Thus, suppose consumers are buying 5000 units at $3. Due to price fixing the price increases to $4 and only 4000 units are sold. In the United States, the measure of damages would be the $1 overcharge times the 4000 units purchased. Of course, no consumer is likely to litigate over $1 per unit but in a class action with larger amounts involved and damages tripled private enforcement might well occur.

On the other hand, leaving out damages associated with the 1000 fewer units sold is a much bigger problem. These former buyers do not have standing. Precisely how one calculates the damages to consumers who stop purchasing a product is not entirely clear. Technically, they lose what economists label consumer surplus. Consumer surplus is the difference between what is paid for the product and the most the consumer is willing to pay. One could think of it as a psychic profit associated with the purchase. Because this damage is associated with a hypothetical transaction giving rise to a psychic benefit, it is very difficult to determine. Consequently the U.S. remedy falls well short of compensation. This may not be important if the threat of suit by those who do purchase is a serious enough deterrent but this may or may not be the case.

In the European Union, overcharge is also the measure of damages. The recovery is equal to single damages, meaning that any deterrent effect is very diluted. To understand this concept, it is important to recall that an action which only allows plaintiffs to recoup the gains of defendants associated with price fixing is one that invites illegal activity. The reasoning is that the probability of recovery is less than 100% and the expected amount recouped would be less than that illegally taken. On balance price fixing would be profitable in the long run. If the damages suffered by those no longer purchasing were added to those of buyers continuing to purchase, the possible total recovery could exceed the gains to those in violation and enhance the deterrent

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51. The evolution of the "overcharge" measure of damages has been examined elsewhere. Jeffrey L. Harrison, *The Lost Profits Measure of Damages in Price Enhancement Cases*, 64 MINN. L. REV. 751, 753, 770–72 (1980).

52. Consumer damages are often very low on a consumer by consumer basis. Thus, the availability of collective redress in the form of class actions is critical for functional standing.

effect. In reality, though, in the absence of an ability to combine claims and the difficulty of quantifying lost consumer surplus mean the probability of private actions by consumers in the European Union for compensation or deterrence purposes is very low.[53] Standing, while broadly defined, cannot be regarded as functional.

B. *Model 2: Price Fixing to Those Reselling*

The analysis is considerably more complex when the purchaser from those fixing prices is itself reselling.[54] In this case, the direct victim is the purchaser of what is called an "intermediate good."[55] The good purchased may be resold to consumers or combined with other inputs to produce a different good which is passed down the chain of distribution to be transformed by downstream firms. As a consequence of the price increase two things happen: The purchaser of the intermediate good decreases the units purchased; because it now purchases less at a higher cost, it produces less and raises its own prices.

In terms of actual harm, the purchasing firm, now paying more for inputs and selling less, is actually harmed by a decrease in profit. Since prices increase, those buying from that firm are also injured. They pay

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53. In more formal language, the prices charged in a market in which purchases are made by consumers without price fixing collusion is compared to one in which price fixing exists. In Figure 1 in the Appendix, before collusion, the price is P1 and the quantity purchased is Q1. The consumer surplus enjoyed by buyers is the area of triangle P1AR. Using the standard model, if price fixing results in an elevation of price to P2, quantity purchased will decline to Q2. Now consumer surplus is P2BR. It has been decreased by the area P1P2BA. In the typical antitrust case, the amount recovered by the affected consumers would be the area P1P2BC. The area P1P2BC is not, however, the same as the total loss to consumers. It leaves out the area ABC, which is the loss to consumers no longer buying the product. As noted above, one might excuse the U.S. system because it does not purport to be primarily aimed at compensation. For the European Union, however, this is a failure to achieve the stated policy goals.

54. In this particular case, it is assumed the resale takes place under imperfectly competitive conditions.

55. In Figure 2 (Appendix 1), D represents the demand that firm faces for its output. For purposes of simplicity, it is assumed that marginal cost and variable cost are the same and equal to C1. It is also assumed that one unit of input translates to one unit of output. Following standard microeconomic theory, the firm sells where its marginal cost and marginal revenue intersect. In the case of C1, this is at Q1. The price charged is the highest consistent with that level of output. Here that price is P1. Now suppose, due to the collusion of suppliers, the average cost and marginal cost curve increase to C2. Again, applying the standard analysis, the new profit maximizing quantity is Q2 and the profit maximizing price is P2. At this point it is useful to note two possible measures of damages. The overcharge, as in the consumer model, is the difference between C1 and C2 and the total recognized damage is the area of rectangle C1C2DE. On the other hand, the actual harm suffered is lost profits. Prior to the price fixing, the profit, including contributions to overhead, was C1P1BF. After price fixing, profit has declined to C2P2AD. There seems to be little question that an actual compensatory award for the direct purchaser would be C1P1BF-C2P2AD.

more for the good and they too purchase less from the direct buyers and their profits decline.[56] In fact, if there are several firms in the chain of distribution, all of them may be negatively affected. Less obvious is the impact on firms that supply the price fixing firms. Firms fixing prices produce less as a result of having raised their own prices and therefore buy less of other inputs for their suppliers. This means these upstream suppliers are also damaged.

In the United States, purchasers from the price fixing firm may recover the amount of the overcharge times three. Those parties are the only ones with standing and the only ones that stand to recover even though actual harm can go up and down the chain of production and distribution. Even if directly purchasing firms pass part of the overcharge to their customers, they collect the full amount of the overcharge. Downstream firms may not recover even if they do pay more for the good or suffer a decrease in profits. In other words, there is no defensive or offensive use of the pass on theory. This simplifies things but means compensation is unlikely. Again, though, compensation is not the goal of U.S. antitrust law.

In the European Union all of this would be treated quite differently. Under the White Paper proposal, standing would evidently extend well beyond the directly affected purchasers. In order to facilitate the ability of remote purchasers to recover damages, the White Paper recommends that they be armed with a rebuttable presumption that the "illegal overcharge was passed onto them in its entirety." Even further, one of the leading cases on the issue of damages, *Manfredi v. Lloyd Adriatico Assicurazioni SpA*, notes that "it follows from the principle of effectiveness and the right of any individual to seek compensation for loss caused by a contract or by conduct liable to restrict or distort competition that injured persons must be able to seek compensation not only for actual loss (*damnum emergens*) but also for loss of profit (*lucrum cessans*) plus interest."[57] Thus, in theory, a truly compensatory model could stretch as far up and down the chain of distribution as possible.

As in the prior model, the E.U. standard with respect to standing is broad but is not functional. It is unlikely to be of consequence with respect to deterrence, which is expected, but it almost certainly will fall short as far as compensation. Again, it is a matter of costs and benefits from the perspective of those who are harmed. In the absence of punitive damages, the maximum recovered is equal to actual harm but the expected recovery is far less. Plaintiffs would be engaged in a

56. These purchasers could be consumers, in which case they suffer a decrease in consumer surplus.

57. Manfredi v. Lloyd Adriatico Assicurazioni SpA, [2006] E.C.R. 1-6619.

difficult process of tracing damages through layers of distribution with each one perhaps finding that its own damages is but a tiny sliver of all the damages caused. And, since the tiny slivers cannot be joined into a class action, the probability of actual compensation drops further. Interestingly, there seems to be no reason to believe that the goal of compensation would be achieved in the proposed E.U. system, which focuses on compensation, than the U.S. system which does not.

C. *Model 3: Monopsony Power and Collusion on the Buying Side of the Market*

A very similar analysis to the one described above can be applied to collusion on the buying side of the market. When buyers collude to achieve lower prices from suppliers they exert what is called "monopsony" power.[58] Typically, when one thinks of buying power it involves the purchase of labor.[59] The condition can and does exist at every level of the production and distribution chain and affects a great variety of inputs.[60] What makes the analysis a bit confusing are the questions of why antitrust policy should oppose the use of buying power and, if so, who has standing. The substantive question of why oppose the use of buying power flows from the fact that those with buying power seek to lower prices. Lower prices, one might reason, leads to lower costs of production throughout the chain of production and distribution, eventually benefitting consumers. The problem with this analysis can be understood fairly easily. When firms collude to force suppliers to charge lower prices, suppliers will sell lower amounts. When lower amounts are supplied, the buyers then produce less of their own output. It is basic economics that lower amounts supplied lead to higher costs. In other words, buying pressure to achieve lower prices does not mean customers of those applying that pressure ultimately benefit.[61]

It is easy to understand the difference between harm caused and compensation if one thinks of the monopsony as the mirror image of the two models described above.[62] In the United States, plaintiffs—in this

58. For a complete discussion of the monopsony problem, see ROGER D. BLAIR & JEFFREY L. HARRISON, MONOPSONY IN LAW AND ECONOMICS (2010).

59. An example would be a so-called company town in which there is but one employer (buyer) of labor.

60. BLAIR & HARRISON, *supra* note 58, at 1–15.

61. *Id.* at 48.

62. The more formal analysis is as follows: demand for the input is determined by how profitable it is for a firm to purchase and use an additional unit of the input. This is marginal revenue product (MRP). *See* Figure 3, Appendix 1. Demand and supply intersect at Q1. The price for the input in this competitive market is P1. If buyers collude, they no longer accept the market determined price but set the price. This means comparing the profitability of each

case sellers faced by powerful buyers—are typically entitled to what can be viewed as the "undercharge" times the number of units that they sell at the lower price. The undercharge is the difference between the price that would have been charged but for the collusion on the buying side of the market and the price actually charged. Again this difference is multiplied by the units actually bought and sold. The problem is that some units that were bought and sold before price fixing are no longer sold. These units were profitable to the seller but they do not lead to a recovery. In effect, the undercharge measure is not compensatory and in the United States it is not intended to be.

It is important to note that the harm is not just that suffered by the sellers to the price fixing firms. Because those sellers now sell less, they are likely to purchase less of whatever inputs they require in their production process. Thus, suppliers to the direct victims are worse off. Plus, since the firms fixing prices sell less and raise their own prices, the impact is also felt down the chain of distribution. All of this would be accounted for if the system aims to be fully compensatory.

The monopsony problem is a relatively new one to U.S. courts and antitrust officials.[63] In the European Union there appears to be even less consideration of monopsony, and it poses many complex problems nearly all of which mean the compensation ideal is unrealistic. For example, a compensatory system would presumably include allowances for pass throughs. Thus, if a firm forced to sell at a lower price can somehow then exact a lower price from its suppliers this would have to be accounted for. And again, all those negatively affected up and down the supply chain would have to demonstrate how their profits were impacted by a price fixing arrangement among firms that could be several tiers removed. Obviously, this is a virtually insurmountable task and one made riskier by the absence of punitive damages and ability to aggregate claims.

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additional unit of input purchased with its marginal cost or marginal factor cost. For all units out to Q2, the marginal revenue product exceeds the marginal factor cost. This net gain ends at Q2, which is now the profit maximizing level of input purchases. The price is set at the *lowest* price consistent with obtaining Q2 units of input or P2. The difference in the price paid per unit after collusion is P2-P1. The quantity sold is Q2. Thus, the measure of damages is P2-P1(Q2), or the area P1P2AB. Depending on the status in direct sellers, this amount may be allocated among plaintiffs at two or more levels. The actual harm resulting from monopsony power is the area P1P2CA. This measure accounts for the impact of sellers who decrease sales as a result of the lower price.

63. The first mention of monopsony power by the U.S. Supreme Court is found in *In re Permian Basin Area Rate Cases*. 390 U.S. 747, 795 n.61 (1968). Although responding to monopsony antitrust issues at earlier dates, the Court's most comprehensive treatment is *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., Inc.*, 549 U.S. 312 (2007).

IX. CONCLUSIONS

A comparison of U.S. and E.U. standards with respect to antitrust injury and antitrust standing is only meaningful in the context of the goals of the two systems of antitrust. Even in that broader context the process is difficult and broad conclusions risky because the relevance of private antitrust actions in the European Union has yet to be determined. Although there are expressions in favor of a substantial expansion, there are significant barriers.

Although each system of private enforcement is concerned at some level with both deterrence and compensation, when faced with choosing, the United States favors a deterrence goal while the European Union favors a compensation goal. There is probably little difference in the antitrust injury requirement between the jurisdictions. On the other hand, the European Union appears to have a more liberal standard with respect to standing. This is, in part, a result of its emphasis on compensation.

Ironically, the United States may, at least in the context of private actions, do a better job with respect to both deterrence and compensation. The key here is not standing and injury but the ability to aggregate claims and the availability of punitive damages. To understand the compensation point it is important to note that compensation is not necessary if deterrence is successful. Thus, in the United States, with a more powerful system of private enforcement, there is what might be called the *ex ante* effect of ensuring the harm does occur in the first place. In effect, treble damages have two results. They create an important incentive for private parties to initiate private actions. Second, that threat and the deterrence it provides can mean there are fewer instances in which compensation would be called for.

The European Union appears to occupy what might be called a no man's land with respect to private enforcement. As it currently stands, private actions are unlikely to have an important compensatory or deterrent effect. The reasons are clear. First, many of the remedies in the European Union have a disgorgement quality. The worst case outcome for colluding firms may be simply to return the unlawful gains. If the probability of detection and liability is less than one, it is in the interest of firms to collude. Second, even when damages are calculated as lost profits, those deserving of compensation may react to small recoveries. This tendency may be offset by increased criminalization or public enforcement, but the announced goals at this point are compensation oriented and that goal is likely unattainable under current functional standing requirements.

Figure 1

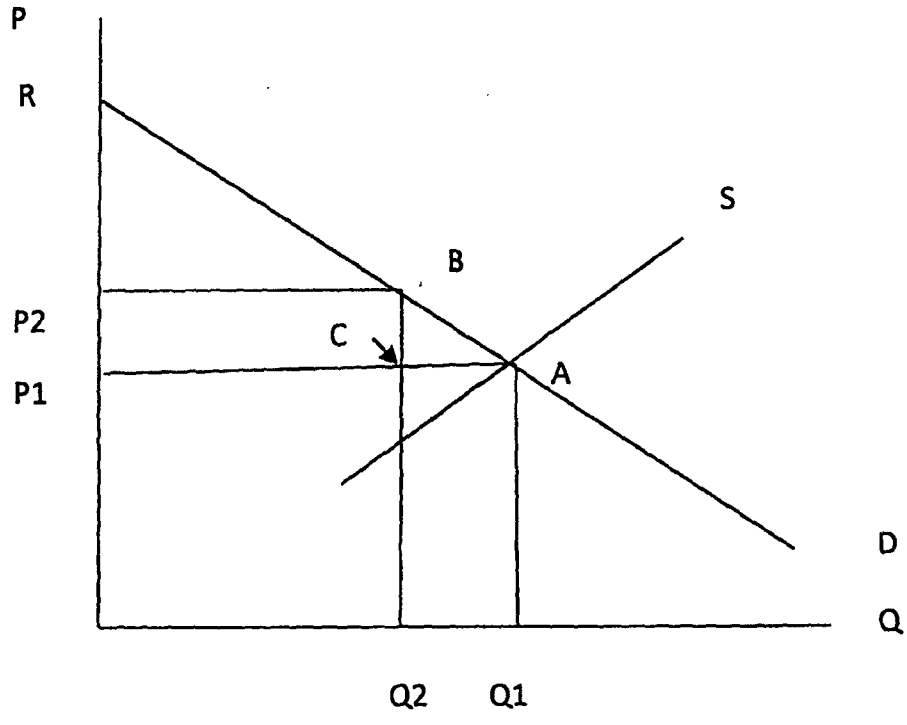

Figure 2