

CLIENT ALERT

California Supreme Court Grants Review of Antitrust Damages "Pass-on" Defense Case

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On November 19, 2008, the California Supreme Court granted plaintiffs' petition for review of the decision of the Court of Appeal of California in *Clayworth v. Pfizer, Inc.* The Court will consider whether the defendant drug companies can use the "pass-on defense" and argue that the plaintiff pharmacies are not entitled to damages because they passed higher drug prices charged in the United States on to their customers.

In the *Clayworth* case, the Court of Appeal addressed the issue of whether the pass-on defense is available in the context of California's Cartwright Act. The plaintiffs in *Clayworth* are a group of retail pharmacies. The defendants are companies who sold pharmaceutical drugs to wholesalers, who then resold the drugs to the plaintiffs. The plaintiffs then resold the drugs to their customers. The majority of the plaintiffs' customers had insurance coverage for the drugs or participated in drug benefit plans. In other words, third parties reimbursed the majority of the plaintiffs' customers for the drugs, thus covering the plaintiffs' acquisition costs in addition to providing the plaintiffs a profit. Even with their uninsured customers, the plaintiffs sometimes resold the drugs at a price incorporating a "dispensing fee," such that the plaintiffs recovered an amount exceeding their acquisition costs.

The plaintiffs alleged that the defendants engaged in price-fixing of drugs. The defendants argued that neither the Cartwright Act nor the California Unfair Competition Law permitted the plaintiffs to recover for any overcharge because the plaintiffs "passed on" any overcharge to their customers. The plaintiffs contended that the defendants could not assert this pass-on defense, relying primarily on the United States Supreme Court's holding in *Hanover Shoe, Inc. v. United Shoe Machinery Corp.* The plaintiffs also relied on the legislative history of the Cartwright Act and on public policy arguments.

The Court of Appeal held that the pass-on defense may be used against a Cartwright Act claim. In coming to this conclusion, the court gave deference to the language of the Act, which provides in relevant part that "[a]ny person who is injured in his or her business or property by reason of anything forbidden or declared unlawful by this chapter, may sue therefore . . . and . . . recover three times the damages sustained by him or her." In particular, the court focused on the meaning of the phrase "damages sustained." Noting that the Act itself does not define the term, the appellate court looked to two cases for guidance, both of which considered damages in the context of the Cartwright Act. According to the court, under *Krigbaum v. Sbarbaro*, a plaintiff may recover under the Cartwright Act only for damages resulting from a restraint in trade, not for damages resulting from the mere "wrongful acts" of the defendant. The court interpreted this to mean that "recovery [i]s only available for the damages the plaintiff *actually* suffered as a result of the antitrust violation." The court then read *Overland P. Co. v. Union L. Co.* as "teach[ing] that a plaintiff who benefits from the alleged [anti-competitive] collusion lacks a Cartwright Act cause of action."

The Court of Appeal ultimately concluded that *Krigbaum* and *Overland* support the notion that, for purposes of the Cartwright Act, "damages sustained" refers to "actual financial loss suffered." In further support of its definition for "damages sustained," the court cited the Judicial Council of California Civil Jury Instruction No. 3440, describing it as "clearly contemplat[ing] that the

damages recoverable under the Cartwright Act are intended to compensate the injured plaintiff for actual monetary loss suffered."

As to the plaintiffs' reliance on *Hanover Shoe*, the Court of Appeal noted that while the Cartwright Act may be "patterned after" the federal Sherman Act, the California Supreme Court has stated that judicial interpretation of the Sherman Act is not dispositive of questions regarding the interpretation of the Cartwright Act. Moreover, the Court of Appeal distinguished *Hanover Shoe* from the instant case, observing that the Supreme Court's holding in *Hanover Shoe* stemmed, in part, from the concern that "establishing the amount of the overcharge passed on to the consumer would present insurmountable evidentiary problems." Such problems of proof were absent in *Clayworth*; because the plaintiff retail pharmacies electronically maintained data on purchases and sales, said data could be "extracted and compiled with relative ease."

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