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The McCarran-Ferguson Act: A Time for Procompetitive Reform

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I. INTRODUCTION

Despite its tremendous national economic importance,[1] the insurance industry generally is not subject to the freely competitive market forces that purport to govern other major segments of the economy. The procompetitive federal policies embodied in the Sherman, Clayton, and Federal Trade Commission Acts are largely inapplicable to the insurance industry by virtue of the McCarran-

1. Although the insurance industry accounts for slightly more than 1% of the gross national income of the United States, it has a much larger impact on the well-being of the nation's economy and citizens. C. KAYSEN & D. TURNER, ANTITRUST POLICY 43 (1959); *see* U.S. BUREAU OF THE CENSUS, A STATISTICAL ABSTRACT OF THE UNITED STATES 379 Table 610 (figures are for the year 1972).

Ferguson Act.[2] Congress has opted for state regulation of the insurance industry—regulation that is neither uniform, unqualifiedly in the consumer interest, or wholly effective. Because recent economic events have emphasized the importance of maintaining an economy that meets the needs of consumers as efficiently as possible,[3] the time is ripe for a review of competition within the insurance industry. The industry's economic importance dictates both that a regulated insurance industry be worth the benefits it provides and that insurance be available to consumers at the lowest possible cost.

In making a case for procompetitive reform, this Note primarily addresses the scheme for regulating prices in the insurance industry. Initially, the historical events that underlie the present regulatory scheme, including judicial interpretation of the McCarran-Ferguson Act, will be examined. Focus then will shift to state insurance regulations and an evaluation of the economic performance of the insurance industry under the present state regulatory system. Finally, alternatives to the present regulatory scheme will be considered, and statutory reform will be proposed.

II. THE MCCARRAN-FERGUSON ACT

A. *Historical Background*

Prior to the American Revolution, there had been few successful attempts to establish insurance enterprises[4] in the United States, and the formation of stock insurance companies was forbidden by British protectionist legislation.[5] After the Revolution, how-

2. McCarran-Ferguson Act, 15 U.S.C. §§ 1011-15 (1970). Ocean marine insurance is exempt from federal antitrust law under § 29(b) of the Merchant Marine Act of 1920, 46 U.S.C. § 885(b) (1970).

3. Emphasis upon consumerism has resulted in the repeal of the antitrust exemptions provided by the McGuire and Miller-Tydings Acts, which authorized so-called "fair trade laws", laws that permitted certain forms of resale price maintenance. Both Acts were repealed by the Act of Dec. 12, 1975, Pub. L. No. 94-145, 89 Stat. 801. 4 TRADE REG. REP. ¶ 25,125, at 30,024 (1976). Consumerism also bas spurred the public demand for increased enforcement of antitrust laws. For example, on December 21, 1974, President Ford signed into law the Antitrust Procedures and Penalties Act which, *inter alia*, provides that a violation of the Sherman Act is now a felony. *See* BNA ANTITRUST & TRADE REG. REP., No. 695, at A-2, D-1 (Jan. 7, 1975). *See generally* Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975) (fee schedules set by state and local bar associations held subject to the Sherman Act); BNA ANTITRUST & TRADE REG. REP., No. 747, at A-1 to A-7 (Jan. 20, 1976).

4. Individual underwriters wrote most insurance, although a few voluntary associations and mutual companies were organized. *See* J. DAY, ECONOMIC REGULATION OF INSURANCE IN THE UNITED STATES 3 (1970) (prepared for the Dep't of Transportation Automobile Insurance and Compensation Study) [hereinafter cited as DAY].

5. Parliament in 1719 legislated an insurance oligopoly by chartering the Royal Exchange Company and the London Assurance Company and by simultaneously outlawing the

ever, the states were free to grant special charters for the incorporation of stock insurance companies.[6] The first such incorporation under a special state charter occurred in 1794 when the Insurance Company of North America was formed in Pennsylvania.[7] Through the 1830's the use of special charters increased, and the potential for state regulation and taxation of insurance companies began to be contemplated.[8] Regulation was designed primarily to maintain company solvency and to prohibit British insurers from doing business rather than to assure fair rates.[9] As competition increased, the seeds of joint rate-making were sewn in the industry,[10] especially among stock fire and casualty companies.

By the 1850's the use of special state charters was abandoned in favor of generally applicable means of incorporation or, for short periods, no requirement that insurance companies be chartered.[11] Nonetheless, with the burgeoning of American industry and commerce the insurance industry expanded, causing a heightened need for governmental regulation. The primary forms taken by the regulation were expanded and particularized reporting requirements and the delegation of regulatory authority, first to already established agencies and later to commissioners or boards specifically established to regulate insurance.[12]

In the latter half of the nineteenth century joint rate-making within the insurance industry dramatically increased for two reasons.[13] First, large fires and wars, unanticipated by the industry, had caused crippling losses to insurers.[14] Secondly, fierce competition drove premium rates dangerously down and caused company

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organization of any other stock companies in His Majesty's dominions. *See* E. PATTERSON, THE INSURANCE COMMISSIONER IN THE UNITED STATES 521-22 (1927) [hereinafter cited as PATTERSON].

6. It is the use of the corporate form in the insurance business to which the development of the industry, the need for government regulations, and the practicability of such regulations have been attributed. *See* S. KIMBALL, INSURANCE AND PUBLIC POLICY 4, 39-40 (1960) [hereinafter cited as KIMBALL].

7. Ch.15229, [1700-1810] Pa. Laws 129. The statute provided for maintenance of loss reserves, limited real estate holdings, required the investment of funds in stocks, and specified a depository hank for the company.

8. *See* DAY, *supra* note 4, at 5.

9. *See Id.* at 4; PATTERSON, *supra* note 5, at 523-24. Taxation took the form of premium taxes, license fees, and stock levies. The required tax filings were the genesis of later state reporting requirements.

10. DAY, *supra* note 4, at 8.

11. *Id.* at 5. *See* KIMBALL, *supra* note 6, at 65-68.

12. *See generally* DAY, *supra* note 4, at 9-13; PATTERSON, *supra* note 5, at 529-37.

13. DAY, *supra* note 4, at 18 & n.54.

14. *See* Kimball & Boyce, *The Adequacy of State Insurance Rate Regulation: The McCarran-Ferguson Act in Historical Perspective*, 56 MICH. L. REV. 545, 546-48 (1958).

failures.[15] In response, the "compact system" evolved as a vehicle for price maintenance, operating primarily at the local and regional levels.[16] Another reaction by the industry to increased competition and to anticorporate sentiment within state legislatures was a concerted lobbying effort directed toward obtaining federal regulation.[17] Because legislative reform was not forthcoming,[18] the industry, and the National Board of Fire Underwriters in particular, sought change through judicial means.[19]

The industry's hope for court-initiated reform rode on the 1868 United States Supreme Court case of *Paul v. Virginia*,[20] which involved two Virginia statutes that required companies not incorporated in Virginia to deposit a bond with the state treasurer and to obtain a license before doing business in the state. The statutes further required the licensing of domestic agents for out-of-state companies. Samuel Paul, a Virginia resident acting on behalf of four New York insurers, had violated the statutes by issuing an insurance policy after being denied a license for his refusal to deposit the bond.[21] Convicted in the state trial court and losing on appeal to the Virginia Supreme Court, Paul, with the support of the National Board of Fire Underwriters, took his case on writ of error to the Supreme Court,[22] where he contended that insurance was a part of interstate commerce and that the Virginia statutes unconstitutionally performed a regulatory function allocated by the commerce clause[23] to Congress rather than to the states.[24] The Court's rejection

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15. DAY, *supra* note 4, at 18.

16. The compact system involved agreements among local agents to abide by rates set by the compact manager, who was employed to oversee the agreements. A local, as opposed to national, combination to fix rates was much less difficult to control and maintain. KIMBALL, *supra* note 6, at 94-96.

17. By the 1860's, the first item on the agenda of meetings of the National Board of Fire Underwriters was "proposing some practicable plan to rid the country of unfair state legislation . . . [and of] securing, if possible, one general law for the government of Insurance Companies throughout the Union." NATIONAL BOARD OF FIRE UNDERWRITERS, JOURNAL OF THE PROCEEDINGS OF THE SECOND ANNUAL MEETING, 25 (1868-69).

18. Several bills were proposed in Congress, but none were enacted. *See* Rose, *State Regulation of Property and Casualty Insurance Rates*, 28 OHIO ST. L.J. 669, 673 (1967).

19. The Committee on Legislation and Taxation of the National Board of Fire Underwriters actively sought a case that would test the constitutionality of state insurance laws. *See* Nekemkis, *Paul v. Virginia: The Need for Re-examination*, 27 GEO. L.J. 519, 526 (1939).

20. 75 U.S. (8 Wall.) 168 (1868).

21. A reconstruction of the events leading up to Paul's refusal to post a bond lends credence to the view that the Underwriter's Agency of New York, along with the insurers whom Paul represented, instructed him to violate the Virginia law. *See* Nekemkis, *supra* note 19, at 526-27.

22. The National Board of Insurance Underwriters supplied Paul with funds and retained two of the ablest lawyers of the time to argue the case. *Id.* at 527-28.

23. U.S. CONST. art. IV, § 2.

24. U.S. CONST. art. I, § 8.

of Paul's contention maintained the insurance industry within the regulatory forum of the states for the next seventy-five years, despite continued industry lobbying and litigation in favor of federal regulation.[25]

During the late nineteenth and early twentieth centuries, state regulation of insurance changed substantially and became more complex as the industry grew. Regulatory functions were invested in special agencies or commissioners in the vast majority of states.[26] From about 1880 through 1900, the compact system for accumulating data and setting rates came under legislative attack.[27] Anticompact legislation proved futile, however, due to lack of enforcement and widespread circumvention on the part of insurance companies.[28] Consequently, some of the states adopted laws permitting joint rate-making but placed it under the supervision of state insurance departments or commissioners.[29] Based primarily on the findings of a New York legislative committee and the National Convention of Insurance Commissioners, which lent credence to the industry claim that unrestricted competition caused rate wars, rate discrimination, and insufficient loss reserves, the new laws established rating bureaus whose members were the insurance companies themselves.[30] Ineffective state enforcement and regulation allowed even supervised joint rate-making to run out of control, however, subjecting the public to price fixing, price maintenance, and boycotts.[31] The evils of the compact system essentially remained unabated.

In the early 1940's the anticompetitive activities of certain rate bureaus and prompting by state authorities caused the Attorney General of the United States to investigate South-Eastern Underwriters Association, a six-state association comprised of over 200 insurance companies. Although the investigation resulted in an indictment against South-Eastern for violations of sections 1 and 2 of the Sherman Act, the indictment was dismissed by a federal district court.[32] The Supreme Court, however, reversed on appeal in *United States v. South-Eastern Underwriters Association*.[33] Mr. Justice

25. DAY, *supra* note 4, at 16. Regarding ocean marine insurance, see note 2 *supra*.

26. By 1919, some 36 states had agencies whose primary function was to regulate insurance. PATTERSON, *supra* note 5, at 536.

27. *See* DAY, *supra* note 4, at 19.

28. *Id.*

29. *See, e.g.*, German Alliance Ins. Co. v. Lewis, 233 U.S. 389, 390-93 (1914) (summarizing Kansas statute permitting joint rate making).

30. DAY, *supra* note 4, at 20-21. *See also* Kimball & Boyce, *supra* note 14, at 551-52.

31. Kimball & Boyce, *supra* note 14, at 552 n.36.

32. United States v. South-Eastern Underwriters Ass'n, 51 F. Supp. 712 (N.D. Ga. 1943).

33. 322 U.S. 533 (1944).

Black, speaking for a majority of four, distinguished *Paul v. Virginia* and its progeny as dealing with the constitutionality of state rather than federal legislation. This distinction was accompanied by the observation that the exclusion of insurance from the ambit of interstate commerce was analytically inconsistent with holdings in other commerce clause cases. Bolstering its analysis with a review of the nature of the insurance business, the Court concluded that insurance was, indeed, a part of interstate commerce. For all practical purposes, *Paul v. Virginia* was overruled,[34] and the insurance industry faced the prospect of vigorous attack under federal antitrust law.

B. *Passage of the McCarran-Ferguson Act*

Although *South-Eastern Underwriters* did not abolish state insurance regulation outright,[35] most people in the insurance industry felt that the dike holding back a flood of federal regulation was on the verge of bursting. The industry immediately sought congressional action to stem the tide. The states also clamored for congressional action because the limit of their regulatory power was unclear and because some insurance companies had already begun to resist the commands of state statutes, which the companies argued were an undue burden on interstate commerce.[36] Eventually draft legislation completed by the National Association of Insurance Commissioners gained congressional support. The draft, introduced by Senators McCarran and Ferguson as a substitute for a stalled bill, eventually was enacted with only minor alterations on March 9, 1945.[37]

The McCarran-Ferguson Act provided, in substance, that the states could continue regulating and taxing the business of insurance[38] and that no act of Congress, other than one specifically relating to the insurance business, should be construed to invalidate, impair, or supersede such state regulatory and tax laws.[39] The insurance industry was given a reprieve from liability under the Sherman, Clayton, Federal Trade Commission, and Robinson-Patman Acts until June 30, 1948.[40] Thereafter, the Sherman, Clayton, and

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34. *See* Note, 23 CHI.-KENT L. REV. 317, 318-19 (1945). Surprisingly, 35 states filed *amicus curiae* briefs on behalf of the defendants. *Id.*

35. *See* Robertson v. California, 328 U.S. 440, 457-58 (1946).

36. *See* Prudential Ins. Co. v. Benjamin, 328 U.S. 408 (1946).

37. Act of Mar. 9, 1945, Pub. L. No. 79-15, 59 Stat. 33 (codified at 15 U.S.C. §§ 1011-15 (1970)).

38. 15 U.S.C. § 1011 (1970).

39. *Id.* § 1012(b).

40. *Id.* § 1013(a).

Federal Trade Commission Acts were not to apply to the business of insurance to the extent that it was regulated by state law.[41] The only exception to these exemptions related to agreements or acts to boycott, coerce, or intimidate, which were to remain subject to the Sherman Act regardless of state regulation.[42]

The legislative scheme, which was enacted hastily and is relatively unsophisticated, created a potential for the resurrection of a number of problems existing before *South-Eastern Underwriters.* The Act effectively mandated a review and redrafting of state legislation governing competition in the insurance industry, but failed to require uniformity of regulation. Furthermore, important terms in the Act were not defined, and standards for the adequacy or enforceability of state laws were not established. Resolution of these and other potential problems, including the continuing specter of creeping federal control arising from the vague language of the McCarran-Ferguson Act, remained to the insurance industry, the state legislatures, and the courts.

C. *Judicial Interpretation of the McCarran-Ferguson Act*

(1) The Boycott, Coercion, and Intimidation Exception

Under section 3(b) of the McCarran Act, boycotts and coercive or intimidating activity on the part of those in the business of insurance remain subject to the prohibitions of the Sherman Act.[43] Since *South-Eastern Underwriters,* which itself involved allegations of a boycott, several other boycott, coercion, and intimidation cases involving insurers have been filed in the federal courts. The impact of this exception on the Act's federal antitrust exemption, however, has been less pronounced than initially might be presumed.

The fact that the exception reserves federal jurisdiction only under the Sherman Act created an unexpected problem subsequent to the 1955 codification of federal antitrust laws in title 15 of the United States Code.[44] In *Professional & Business Men's Life Insurance Co. v. Banker's Life Co.,*[45] a 1958 boycott case, the Montana federal district court determined that the private treble damage remedy originally provided by section 7 of the Sherman Act would not be available to plaintiffs in boycott, coercion, or intimidation

41. *Id.* § 1012(b).
42. *Id.* § 1013(b).
43. *Id.*
44. The Sherman Act became §§ 1-7 of Title 15, while §§ 12-27 and 44 are properly the Clayton Act.
45. 163 F. Supp. 274 (D. Mont. 1958).

cases under the McCarran exceptions if the alleged activities took place after July 7, 1956. The rationale for this startling conclusion was that when the codification of federal antitrust laws occurred, Congress retained the grant of a private action for treble damages from section 4 of the Clayton Act, while excluding the separate grant of a private treble damage action, which was contained in the Sherman Act.[46] Since the two provisions were identical in effect, the Sherman treble damage provision was repealed as surplusage on July 7, 1955.[47] Applying a long-standing canon of statutory construction, the court reasoned that section 3(b) of the McCarran Act adopted the Sherman Act as it existed in 1945 when the McCarran Act was passed but did not adopt additions or modifications to the Sherman Act made subsequent to 1945. The court thus concluded that, insofar as section 3(b) of the McCarran Act is concerned, the repeal of section 7 of the Sherman Act destroyed the treble damage remedy for cases of boycott, coercion, and intimidation. The incorporation of section 4 of the Clayton Act into title 15 of the United States Code was found ineffective to restore the remedy.[48] A subsequent district court decision, *Monarch Life Insurance Co. v. Loyal Protective Life Insurance Co.*,[49] followed the reasoning in *Banker's Life*, but was reversed by the Second Circuit in 1963.[50] Asserting that the Montana District Court's statutory interpretation was too literal and produced drastic consequences, the Second Circuit determined that the repeal of section 7 of the Sherman Act was "mere Congressional housekeeping." Somewhat metaphysically, but certainly more in harmony with the intent of Congress, the court concluded that the Clayton Act's treble damage provision was so basic to the effective enforcement of the Sherman Act that it should be read by implication into section 3(b) of the McCarran Act. The logic of this valiant attempt to patch up the disarray created by the "congressional housekeeping" of 1955 is by no means unexceptionable. It is also not clear that it was successful. Due to the seemingly unquestioning acceptance by federal courts of the availability of treble damages in most of the other post-1955 cases dealing with boycott, coercion, or intimidation, the issue has not been probed further.[51] Section 3(b) of the McCarran Act remains unamended,

46. Section 15 of 15 U.S.C. is technically the Clayton Act's treble damage provision. *Id.* at 283, 292-95.

47. Act of July 7, 1955, ch. 283, § 3, 69 Stat. 282.

48. 163 F. Supp. at 292-95.

49. 217 F. Supp. 210 (S.D.N.Y. 1963).

50. 326 F.2d 841 (2d Cir. 1963), *cert. denied*, 376 U.S. 952 (1964).

51. *See, e.g.*, Cooperativa de Seguros Multiples de Puerto Rico v. San Juan, 289 F. Supp. 983, 986 (D.P.R. 1968).

however, and whether an insurer who is found liable for coercion, boycott, or intimidation successfully can avoid the bite of treble damages remains unresolved.

Another rather astonishing development has been the judicial interpretation of who can bring the Sherman suits authorized by section 3(b). One court has stated that section 3(b) "was placed in the legislation to protect insurance agents from the issuance by insurance companies of a 'black list,' which would name companies or agents which were beyond the *pale*."[52] This theory, grounded in part on the nature of *South-Eastern Underwriters* and in part on the legislative debates on the McCarran Act, was the basis for denying the applicability of section 3(b) in the contest of an alleged combination or conspiracy to coerce policyholders in *Addrisi v. Equitable Life Assurance Society of the United States*.[53] In *Addrisi* plaintiff alleged that defendant tied an excessively costly life insurance policy to home loans offered to prospective policyholders at rates below the market for conventional mortgages. The court dismissed his claim, stating that

> it is evident from an examination of the legislative history behind § 1013(b) [section 3(b) of the McCarran Act] that the intent of Congress was to reserve unto the reach of the Sherman Act only a narrow area of restraint of trade activity among those in the business of insurance, namely, antitrust acts among insurance companies and agents for the purpose of boycott or coercion among insurance companies and agents.[54]

Continuing, the court stated:

> We are not concerned with the meaning or the language of the words "acts of coercion" as used in § 1013(b) per se, but only of what class of persons or business relationship is protected from "acts of coercion" under the Sherman Act through the reserving thrust of § 1013(b).[55]

Apparently, under this line of authority, the only private plaintiffs who may avail themselves of the section 3(b) exception are insurance companies and agents. Policyholders rarely if ever succeed in suits under 3(b).[56] For the most part, however, dismissals have been

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52. Transnational Ins. Co. v. Rosenlund, 261 F. Supp. 12, 26 (D. Ore. 1966).

53. 503 F.2d 725 (1974), *cert. denied*, 420 U.S. 929 (1975).

54. *Id.* at 728-29.

55. *Id.* at 729.

56. The problem of the availability of the boycott, coercion, and intimidation exception to insurance consumers is similar to the standing problems of consumers under § 4 of the Clayton Act. A recent case study dealing with § 4 states:

> Such persons [consumers] suffer a pocketbook injury from antitrust violations, but they are not the "targets" of anticompetitive practices. The "target area" test arose as a means of limiting the class of potential treble-damage plaintiffs to those who could most adequately vindicate the purposes of the antitrust laws. To attain standing a person

based on failure to allege or prove sufficiently the existence of boycott, coercion, or intimidation.[57] Overall, section 3(b) has proved to be of little help to insurance consumers.

The government, however, which theoretically acts for consumers generally, has enforced the antitrust liability reserved by section 3(b). The Department of Justice has brought two actions against insurance agents' associations that boycotted mutual insurance companies and their agents, nonmember agents, cut-rate insurers, and direct-selling insurers.[58] The alleged purpose of the boycotts was to promote the stock insurance company and independent agency concepts. In both cases, federal district courts held that the McCarran Act exemption from liability under the Sherman Act was inapplicable by virtue of section 3(b). These cases, therefore, established that the government is a proper plaintiff and that insurance agents' organizations may be proper defendants in suits within the ambit of the 3(b) exception.

The section 3(b) cases involving insurance companies or insurance agents as plaintiffs also usually have been dismissed or won by defendants on motions for summary judgment due to failure to allege specifically or prove sufficiently boycott, coercion, or intimidation.[59] Despite this overall lack of success on the part of plaintiffs in section 3(b) cases, it seems clearly established that the term "boycott" in the McCarran Act means the same as in the Sherman Act.[60] Additionally, price fixing, even when allowed or required by state law in the form of rating boards, probably should be actionable by virtue of section 3(b) when boycott, coercion, or intimidation are involved, despite the failure of most or all such actions.[61]

> (whether corporation or individual) must be one against whom the conspiracy is aimed. Or, put in plutonomic terms, the complainant must show that he is within that sector of the economy which is endangered by a breakdown of competitive conditions in a particular industry.

Jeffrey v. Southwestern Bell, 518 F.2d 1129, 1131 (5th Cir. 1975).

57. *See* Romac Resources, Inc. v. Hartford Accident & Indem. Co., 378 F. Supp. 543 (D. Conn. 1974), *aff'd*, 513 F.2d 102 (2d Cir. 1975); Steingart v. Equitable Life Assurance Soc'y of the United States, 366 F. Supp. 790 (S.D.N.Y. 1973); Holly Springs Funeral Home, Inc. v. United Funeral Serv., Inc., 303 F. Supp. 128 (N.D. Miss. 1969).

58. *See* United States v. Insurance Bd., 144 F. Supp. 684 (N.D. Ohio 1956), 188 F. Supp. 949 (N.D. Ohio 1960); United States v. New Orleans Ins. Exch., 148 F. Supp. 915 (E.D. La.), *aff'd per curiam*, 355 U.S. 22 (1957).

59. *See* American Family Life Assurance Co. v. Blue Cross, 486 F.2d 225 (5th Cir. 1973), *aff'g* 346 F. Supp. 267 (S.D. Fla. 1972); American Family Life Assurance Co. v. Aetna Life Ins. Co., 368 F. Supp. 859 (N.D. Ga. 1973); Travelers Ins. Co. v. Blue Cross, 361 F. Supp. 774 (W.D. Pa. 1972), *aff'd*, 481 F.2d 80 (3rd Cir.), *cert. denied*, 414 U.S. 1093 (1973).

60. Professional Adjusting Systems, Inc. v. General Adjustment Bureau, 64 F.R.D. 35, 43 (S.D.N.Y. 1974); *see* Cooperativa de Serguros Multiples de Puerto Rico v. San Juan, 289 F. Supp. 983 (D.P.R. 1968).

61. *See, e.g.*, Allstate Ins. Co. v. Lanier, 242 F. Supp. 73 (E.D.N.C. 1965), *aff'd*, 361

(2) The Meaning of "Business of Insurance"

Section 2(b) of the McCarran-Ferguson Act,[62] which states that federal law shall not displace any state law enacted to tax or regulate the "business of insurance" unless the federal law specifically governs that business, is the primary exemptive provision of the Act. The meaning of the term "business of insurance" is therefore crucial in determining what specific activities are within the scope of the exemption.

With the exception of a few cases,[63] for more than twenty years after the passage of the McCarran Act courts generally assumed that the term encompassed virtually all activities in which insurance companies and agents engaged.[64] In 1969, however, the Supreme Court held in *SEC v. National Securities, Inc.*,[65] that "business of insurance" does not encompass every activity in which insurers engage. The Court gave examples of activities that were sub-

F.2d 870 (4th Cir.), *cert. denied*, 385 U.S. 930 (1966). The *Lanier* case came in the wake of a 1961 Senate Judiciary Committee Report, which stated: "The requirement of several State statutes for mandatory bureau memberships substantially lessens competition and appears to be in conflict with the McCarran Act." SENATE COMM. ON THE JUDICIARY AND SUBCOMM. ON ANTITRUST AND MONOPOLY, THE INSURANCE INDUSTRY, INSURANCE: RATES, RATING ORGANIZATIONS AND STATE RATE REGULATION, S. REP. No. 831, 87th Cong., 1st Sess. 77 (1961). Nonetheless, the Fourth Circuit upheld just such a statute in *Lanier*. The case was brought by independent auto liability insurers who wished to charge rates below the minimums set by the North Carolina Automobile Rate Commission, membership in which is made mandatory by North Carolina law. Plaintiffs argued tbat North Carolina had gone beyond what was mandated by the McCarran Act and, in effect, that the state itself was engaged in a boycott in violation of the Sherman Act. The Justice Department as *amicus curiae*, on the other hand, argued that the North Carolina Insurance Commissioner did not have the power to prevent bureau members from conspiring to coerce and intimidate other members to agree to favorable rates and, therefore, that the state's regulation did not meet McCarran Act standards. In upholding the North Carolina regulatory scheme, the Fourth Circuit relied primarily on Parker v. Brown, 317 U.S. 341 (1943), for the proposition that the state's authorization and active supervision of insurance rate-making was not subject to challenge under federal antitrust law.

62. 15 U.S.C. § 1012(b) (1970).

63. In a 1959 case, SEC v. Variable Annuity Life Ins. Co. of America, 359 U.S. 65 (1959), the Supreme Court held that the issuance of variable annuity contracts was not a part of the business of insurance. In 1960 a district court held that the financing of an insurance company by an agency which sold its policies was not within the term "business of insurance." United States v. Meade, 179 F. Supp. 868 (S.D. Ind. 1960). Another district court, in 1963, found that an insurance company's securing for particular automobile glass dealers the sales and installation jobs required by the company's claimants was not within the scope of "business of insurance." Hill v. National Auto Glass Co., 293 F. Supp. 295 (N.D. Calif. 1968).

64. *See* Transnational Ins. Co. v. Rosenlund, 261 F. Supp. 12 (D. Ore. 1966); Professional & Bus. Men's Life Ins. Co. v. Banker's Life Co., 163 F. Supp. 274 (D. Mont. 1958); Miley v. John Hancock Mut. Life Ins. Co., 148 F. Supp. 299 (D. Mass.), *aff'd*, 242 F.2d 758 (1st Cir.), *cert. denied*, 355 U.S. 828 (1957).

65. 393 U.S. 453 (1969). The case involved allegations of fraud under the Securities Exchange Act of 1934 arising from the merger of two insurance companies with the approval of the Arizona Insurance Commissioner.

sumed within "business of insurance;" these included rate setting, policy sales and advertising, and company and agent licensing. Speaking more generally, the Court stated:

> The relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement—these were the core of the "business of insurance." Undoubtedly, other activities of insurance companies relate so closely to their [insurance companies'] status as reliable insurers that they too must be placed in the same class.[66]

Admitting that the exact scope of the term could not be defined precisely, the Court asserted that its focus was on the relationship of insurer and insured. The Court found that an Arizona law granting authority for approval of a merger, though pertaining solely to insurance companies, regulated the relationship between insurance companies and their stockholders rather than their insureds; in essence, the law regulated securities but not the "business of insurance." The McCarran exemption was therefore inapplicable.

The holding in *National Securities* establishes that the term "business of insurance" in section 2(b) of the McCarran Act does not include insurance company mergers.[67] The dictum, which suggests what the term does include, has been a persuasive influence in subsequent cases. Courts have held that the term has the same meaning throughout the Act as it has in section 2(b) and that it does not encompass stealing an insurance company's agents or trade secrets, the "twisting" of policyholders, or the usurpation of its agency organization by another insurance company.[68] Contracts between health insurers and hospitals setting the fees for medical services rendered to insureds,[69] title search services performed prior to the issuance of title insurance,[70] and the appropriation by one insurance company on another's name[71] have been found to be part of the business of insurance. In addition, insurance services provided

66. *Id.* at 460.

67. *See* American Gen. Ins. Co. v. FTC, 359 F. Supp. 887 (S.D. Tex. 1973), *aff'd*, 496 F.2d 197 (5th Cir. 1974). *See also* Hamilton Life Ins. Co. v. Republic Nat'l Life Ins. Co., 408 F.2d 606 (2d Cir. 1969).

68. *See* American Family Life Assurance Co. v. Planned Marketing Assoc., Inc., 389 F. Supp. 1141 (E.D. Va. 1974). "Twisting," in the jargon of the industry, occurs when one insurance company tries to obtain business from another company's policyholders hy convincing them to terminate their coverage with the latter in favor of coverage with the former. *Id.* at 1143.

69. Travelers Ins. Co. v. Blue Cross, 361 F. Supp. 774 (W.D. Pa. 1972), *aff'd*, 481 F.2d 80 (3rd Cir.), *cert. denied*, 414 U.S. 1093 (1973).

70. Commander Leasing Co. v. Transamerica Title Ins. Co., 477 F.2d 77 (10th Cir. 1973); Schwartz v. Commonwealth Land Title Ins. Co., 374 F. Supp. 564, 383 F. Supp. 302 (E.D. Pa. 1974).

71. Sanborn v. Palm, 336 F. Supp. 222 (S.D. Tex. 1971).

under another name have been found to be within the business of insurance.[72] On the other hand, it seems reasonably clear in light of more recent cases that neither the making of loans in connection with the sale of various types of insurance,[73] the purchase by insurance companies of the names of potential policyholders,[74] nor the procuring by a burial insurer of funeral home services or supplies for insureds[75] are within the business of insurance. In sum, although the breadth of the exemption granted by section 2(b) of the McCarran-Ferguson Act has been narrowed by virtue of the judicial interpretation of the term "business of insurance," the policyholder has not benefitted materially because the relationship between insurer and insured and price fixing remains within the scope of the McCarran exemption.

(3) The Meaning of "Regulated by State Law"

The proviso to section 2(b) of the McCarran Act states that after June 30, 1948, the Sherman, Clayton, and Federal Trade Commission Acts "shall be applicable to the business of insurance to the extent that such business is not *regulated by state law*."[76] Unanswered by the Act are the questions which state is the relevant state for regulatory purposes and what constitutes "regulation." The answers are important since they essentially determine a federal court's power to provide a remedy when the activities of those in the business of insurance are challenged under federal antitrust law.

The landmark decision with regard to which state is relevant for regulatory purposes is *FTC v. Travelers Health Association*,[77] which involved a Federal Trade Commission cease and desist order that prohibited a company licensed only in Nebraska and Virginia from making deceptive statements in circulars distributed in the conduct of its nationwide mail order insurance business. Relying on the McCarran Act exemption in light of a Nebraska statute barring unfair and deceptive insurance practices, defendant managed to have the order set aside by the Eighth Circuit. The Supreme Court vacated the judgment, stating:

72. *See* American Family Life Assurance Co. v. Blue Cross, 486 F.2d 225 (5th Cir. 1973), *aff'g* 346 F. Supp. 267 (S.D. Fla. 1972).

73. *See* Fry v. John Hancock Mut. Life Ins. Co., 355 F. Supp. 1151 (N.D. Tex. 1973).

74. *See* DeVoto v. Pacific Fidelity Life Ins. Co., 354 F. Supp. 874 (N.D. Cal. 1973), *rev'd in part*, 516 F.2d 1 (9th Cir. 1975).

75. *See* Battle v. Liberty Nat'l Life Ins. Co., 493 F.2d 39 (5th Cir.), *cert denied*, 419 U.S. 1110 (1974); Romac Resources, Inc. v. Hartford Accident and Indem. Co., 378 F. Supp. 543 (D. Conn. 1974), *aff'd*, 513 F.2d 102 (2d Cir. 1975).

76. 15 U.S.C. § 1012(b) (1970) (emphasis added).

77. 362 U.S. 293 (1960).

> In this case the state regulation relied on to displace the federal law is not the protective legislation of the States whose citizens are the targets of the advertising practices in question. Rather, we are asked to hold that the McCarran-Ferguson Act operates to oust the Commission of jurisdiction by reason of a single State's attempted regulation of its domiciliary's extraterritorial activities. But we cannot believe that this kind of law of a single State takes from the residents of every other State the protection of the Federal Trade Commission Act. In our opinion the state regulation which Congress provided should operate to displace this federal law means regulation by the State in which the deception is practiced and has its impact.[78]

Although the Court referred only to the Federal Trade Commission Act, the holding should apply for the Sherman and Clayton Acts as well.[79] The holding seems eminently reasonable and fairly should serve the interest of consumers.

The reasonableness of judicial pronouncements concerning what constitutes "state regulation" is less certain. In *FTC v. National Casualty Co.*,[80] a 1958 case involving another cease and desist order directed toward deceptive insurance practices, the Supreme Court interpreted section 2(b)'s "regulation." In response to the Federal Trade Commission's argument that a state statute prohibiting in general terms unfair and deceptive insurance practices was too inchoate to be "regulation" until it had been administratively elaborated into objective and applicable standards for conduct, the Court stated, "assuming there is some difference in the McCarran-Ferguson Act between 'legislation' and 'regulation,' nothing in the language of that Act or its legislative history supports the distinctions drawn by petitioner."[81] This statement is indicative of the offhanded treatment given by the federal courts to the "regulation" issue.

The argument that "regulation" means effective regulation, or more than mere legislation, has been made repeatedly but to no avail. An exemplary case in this regard is *Ohio AFL-CIO v. Insurance Rating Board*,[82] in which plaintiff alleged that defendants had violated the Sherman Act by contracting, combining, and conspiring to fix prices and dictate terms for the sale of auto insurance in several states. Despite evidence that the Ohio Insurance Commissioner had abdicated his supervisory responsibilities over rate making, permitted insurers essentially to regulate themselves, and

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78. *Id.* at 297-99.

79. *See* Steingart v. Equitable Life Assurance Soc'y of the United States, 366 F. Supp. 790 (S.D.N.Y. 1973).

80. 357 U.S. 560 (1958).

81. *Id.* at 564-65.

82. 451 F.2d 1178 (6th Cir. 1971), *cert. denied*, 409 U.S. 917 (1972) (Douglas, J., dissenting).

did not even employ the services of an actuary, the Sixth Circuit found that sufficient regulation existed to support the McCarran Act exemption. Another Court of Appeals case, *Crawford v. American Title Insurance Co.*,[83] held that even though the Alabama Insurance Commissioner by statute expressly was denied authority to supervise the making of title insurance rates, the state's regulation of insurance generally was sufficient to bring the title insurance industry within the McCarran exemption. Another case held that laxness on the part of the Pennsylvania Insurance Commissioner in allowing title insurance companies to collect unapproved revenues did not constitute nonregulation.[84] Federal courts frequently have found seemingly ineffective regulation, or only generally applicable legislation, to be "regulation" for purposes of the McCarran Act.[85] So far as can be determined, only one court has ventured to assert, even in dicta, that state regulation should be effective if it is to exempt insurance companies from federal antitrust law.[86] Not only insurance statutes but also state antitrust,[87] business, or commercial laws,[88] if they apply to the insurance industry, can trigger the McCarran Act's exemptions, even though the statutes do not contain prohibitions or remedies similar to those in federal antitrust laws.[89]

Thus the judicial interpretation of the term "regulation" in section 2(b) of the McCarran Act suggests that the antitrust exemption will be available to the insurance industry as long as state regulatory laws are on the books. Except when the regulatory scheme amounts to a gross sham or pretence, the courts will not inquire into the actual efficacy of a state's supervisory control over the insurance industry. As at least one observer has said, the consumer deserves better.[90]

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83. 518 F.2d 217 (5th Cir. 1975).

84. Schwartz v. Commonwealth Land Title Ins. Co., 384 F. Supp. 302 (E.D. Pa. 1974).

85. *See, e.g.*, Lawyers Title Co. v. St. Paul Title Ins. Corp., 526 F.2d 795 (8th Cir. 1975); California League of Indep. Ins. Producers v. Aetna Cas. & Sur. Co., 175 F. Supp. 857 (N.D. Cal. 1959); Miley v. John Hancock Mut. Life Ins. Co., 148 F. Supp. 299 (D. Mass.), *aff'd*, 242 F.2d 758 (1st Cir. 1957).

86. Fleming v. Travelers Indem. Co., 324 F. Supp. 1404, 1406 (D. Mass. 1971).

87. *See* Steingart v. Equitable Life Assurance Soc'y of the United States, 366 F. Supp. 790 (S.D.N.Y. 1973).

88. *See* Sanborn v. Palm, 336 F. Supp. 222 (S.D. Tex. 1971).

89. *See* Prudential Ins. Co. v. Benjamin, 328 U.S. 408, 431 (1946); Transnational Ins. Co. v. Rosenlund, 261 F. Supp. 12 (D. Ore. 1966).

90. Comment, *State Regulation Under the McCarran Act*, 47 TUL. L. REV. 1069, 1084 (1973).

D. *Conclusion*

Historically, the insurance industry in the United States has remained free of many of the antitrust prohibitions to which most other businesses are subject. It is arguable on the basis of its history through 1945 that the industry, or certain elements within it, successfully has counterbalanced the federal and state governments in order to maintain a privileged status under antitrust laws.[91] When the pressures of state legislation grew stronger in the second half of the nineteenth and early twentieth centuries, federal regulation was sought. When the prospect of more stringent federal regulation loomed, swift action was taken to avoid it. Under the McCarran-Ferguson Act, the business of insurance presently is exempted from federal antitrust law so long as it is regulated by the states, with the exception of retained federal jurisdiction under the Sherman Act for activities constituting boycott, coercion, and intimidation. The courts have limited the scope of the McCarran Act by virtue of their narrow construction of the term "business of insurance." The contention on the part of some that the McCarran exemption is shrinking drastically[92] or that it is chimerical[93] is greatly overstated. The reserved jurisdiction of the Sherman Act as a remedy for boycott, coercion, and intimidation has benefitted the general public to some degree by virtue of a few successful suits prosecuted by the Justice Department, but relief under this exception appears to be unavailable to individual consumer plaintiffs. The federal courts have been rather indiscriminate in their acceptance of seemingly unenforced or unenforceable state legislation as sufficient regulation to preempt the general application of federal antitrust law. Whatever stimuli toward competition and against unfair and deceptive practices exist in the insurance industry are largely not the results of federal policy. If the consumer is to receive substantial protection from price-fixing and other anticompetitive practices, the protection must come from state law.

III. Competition in the Insurance Industry

A. *State Regulation of Competition*

State insurance regulation may be broadly divided into two categories. The first generally encompasses those laws that are di-

91. *See* Day, *supra* note 4, at 17.

92. *See generally* Note, *Federal Regulation of Insurance Companies: The Disappearing McCarran Act Exemption*, 1973 Duke L.J. 1340.

93. *See generally* Atwell, *The McCarran-Ferguson Act—A Deceptive Panacea*, 5 The Forum (A.B.A.) 339 (1970).

rected toward protecting the insurance fund so that a policyholder can be secure in his reliance on his insurer's ability to pay its obligations. An assumption underlying this Note is that such regulation, despite its imperfection and effect on competition, is both socially and economically desirable. Thus the problems with state regulation aimed at ensuring the financial reliability and solvency of insurance companies[94] will not be considered here. Rather, this section of the Note will outline the second category of state insurance regulation, which governs pricing and business practices more directly affecting competition. Some general problems relating to state regulation also will be discussed. This section and the following section, which assesses the competitive performance of the insurance industry under state regulation, are further limited in that they analyze only the nonlife segment of the industry. Significant differences in price competition and regulation in particular warrant the exclusion of life insurance companies from consideration.[95]

(1) State Rating Laws

State insurance laws permitting the joint making of rates, but particularly of fire, casualty, and surety rates, in the majority of states owe their existence and form largely to two model rating laws that were drafted shortly after the passage of the McCarran-Ferguson Act. Motivation for drafting these laws came from the uncertain meaning of "regulation" in section 2(b) of the Act and from the desire on the part of the states and the industry to make certain that state regulation would be sufficient to maintain the McCarran exemption after the three year moratorium from federal

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94. The states vary considerably, for example, in terms of the absolute capital requirements that must be met hefore an insurer can commence writing policies. *See generally* R. HENSLEY, COMPETITION, REGULATION, AND THE PUBLIC INTEREST IN NONLIFE INSURANCE 48-52 (1962) [hereinafter cited as HENSLEY]. Other areas, such as regulation of reserves, have been criticized. *See, e.g.*, Belth, *Life Insurance Reserves and the Regulatory Process*, in INSURANCE, GOVERNMENT, AND SOCIAL POLICY 95 (S. Kimball and H. Denenherg eds. 1969).

95. Rose, *supra* note 18, at 702 n.165 states:

> Life insurance rates are fixed by the companies on the basis of mortality experience, insurance assumption, and expense assumptions, together with competition. No rating bureaus or other industry agreements exist concerning rates. State reserve requirements take care of solvency problems. All life insurers do not, however, use the same pure premiums. Insurers which do not pay dividends use lower pure premiums than the others. Also insurers may use one of several mortality tables.

Price competition among life insurers has been found to be considerable. In addition, regulators distinguish hetween the life and nonlife segments of the insurance industry. *See generally* HENSLEY, *supra* note 94, at 5-6; Belth, *Life Insurance Price Measurement*, 57 KY. L.J. 688, 709 (1969).

antitrust enforcement expired in 1948.[96] The model rating laws were drafted by the National Association of Insurance Commissioners (NAIC), aided by the so-called All-Industry Committee (AIC), which represented nineteen insurance industry organizations.[97] A number of fundamental and controversial problems were confronted during the course of the drafting, including how much regulation was required, whether all rates or only jointly made rates should be subject to state administrative supervision, and whether regulation should take the form of prior approval or subsequent disapproval of rates.[98] The factions generally in opposition during the deliberations were the independent insurers and those more powerful insurers who preferred the bureau or compact system.[99] Through some degree of compromise, but despite lingering dissent from the independents, one bill for regulating casualty and surety rates and another for fire and marine rates were endorsed by the NAIC in June of 1946.[100]

The stated purpose of the two essentially identical model bills was "to promote the public welfare by regulating insurance rates to the end that they shall not be excessive, inadequate, or unfairly discriminatory, and to authorize and regulate cooperative action among insurors in rate making and in other matters . . . ."[101] The bills provided for the licensure and supervision of rating bureaus and rate advisory organizations,[102] which were to allow nonmembers to become subscribers and were to provide their rating services without discrimination to both members and subscribers.[103] The organizations could act cooperatively in setting rates but could not adopt rules prohibiting or regulating the payment of dividends or the return of unabsorbed premiums by subscribers or members.[104] All rates governed by the bills were to be set on the basis of past and

96. *See* Mertz, *The First Twenty Years—A Case Law Commentary on Insurance Regulation Under the Commerce Clause*, in ABA SECTION OF INSURANCE, NEGLIGENCE AND COMPENSATION LAW, 153, 161-65 (1963-1964).

97. *Id.* at 161 n.31.

98. *Id.* at 162-65.

99. *See* Rose, *supra* note 18, at 696-704. *See also* Mertz, *supra* note 96, at 162-65; Moser, *Operation of Independents Under the Rate Regulatory Pattern*, 15 LAW & CONTEMP. PROB. 523, 527-29 (1950).

100. The text of bills is found in PROCEEDINGS OF THE NATIONAL ASS'N OF INSURANCE COMMISSIONERS, 78th Sess., at 397-422 (1947) [hereinafter cited as NAIC PROCEEDINGS].

101. Casualty and Surety Rate Regulatory Bill § 1, *id.* at 397-98; Fire, Marine and Inland Marine Rate Regulatory Bill § 1, *id.* at 410.

102. Casualty and Surety Rate Regulatory Bill §§ 6-15, *id.* at 401-07; Fire, Marine and Inland Marine Rate Regulatory Bill §§ 6-13, *id.* at 414-19.

103. Casualty and Surety Rate Regulatory Bill § 6, *id.* at 401-03; Fire Marine and Inland Marine Rate Regulatory Bill § 6, *id.* at 414-15.

104. *See* note 6 *supra*.

prospective expenses and loss experience within the state or nationwide, a reasonable profit and contingency margin, the amount of dividends and returns of unabsorbed premiums, and other relevant factors.[105] All rates were to be filed with supporting data, either independently or by rating bureaus on behalf of their members and subscribers.[106] In general, newly filed rates were to go into effect if not disapproved during a fifteen-day waiting period, which could be extended for an additional fifteen days upon written notice by a state insurance commissioner.[107] Upon disapproval of a filing during the permissible thirty-day waiting period, a commissioner had to give the reasons therefor.[108] If a commissioner wished to set aside a filing after the thirty-day review period, he had to hold a hearing upon notice to all parties concerned, after which he could issue an order stating reasons for disapproving the filing and setting a date after which the rate would be ineffective.[109] Under the laws, any person or organization, except the filer, aggrieved with respect to a filing was entitled to request a hearing before the commissioner.[110] Members of and subscribers to rating organizations were required to comply with their bureau's rate filings, except that they could "make written application to the (commissioner) for permission to file a uniform percentage decrease or increase to be applied to the premiums produced by the rating system. . . ."[111] These so-called deviations, which were limited to one year, had to be supported by appropriate data.[112] In addition, both the application and supporting data had to be provided to the rating bureau with which the deviator was affiliated.[113] The rating bureau then had the right to a hearing before the commissioner at which it could, in the status of an aggrieved party, argue against approval of the deviation.[114] Finally, the bills permitted state insurance commissioners to use rating organizations as an aid in gathering information necessary in

105. Casualty and Surety Rate Regulatory Bill § 3, NAIC PROCEEDINGS, *supra* note 100, at 398-99; Fire, Marine and Inland Marine Rate Regulatory Bill § 3, *id.* at 411-13.

106. Casualty and Surety Rate Regulatory Bill § 4, *id.* at 399-400; Fire, Marine and Inland Marine Rate Regulatory Bill § 4, *id.* at 412-13.

107. *See* note 9 *supra.*

108. Casualty and Surety Rate Regulatory Bill § 5, NAIC PROCEEDINGS, *supra* note 100, at 400-01; Fire, Marine and Inland Marine Rate Regulatory Bill § 5, *id.* at 413-14.

109. *See* note 9 *supra.*

110. *Id.*

111. Casualty and Surety Rate Regulatory Bill § 7, NAIC PROCEEDINGS, *supra* note 100, at 403-04; Fire, Marine and Inland Marine Rate Regulatory Bill § 7, *id.* at 416.

112. *See* materials cited in note 12 *supra.*

113. *Id.*

114. *Id.*

performing the regulatory function,[115] and contained procedural and punitive provisions.[116]

Even from this summary review of the model bills, it is apparent that the interests favoring collective rate making got most of what they wanted in the course of the NAIC/AIC deliberations. Although the operation of the independents was permitted, both independently and jointly made rates were governed by the filing scheme. Furthermore, the rating bureau concept, embodying the historic fear that open competition engendered rate wars and company failures, was legitimized.[117] Thus the paradigms for post-McCarran Act state rate regulations perpetuated to some degree, either explicitly or implicitly, the anticompetitive spirit that was widespread in the insurance industry prior to *South-Eastern Underwriters*. In retrospect, the deliberations over the model bills, much as with the McCarran Act itself, "reflected the need for hasty compromises, with implications not clearly understood."[118] The great majority of states, however, enacted rate regulatory statutes patterned exactly or substantially on the model bills,[119] almost all of which remain in force today.[120] In a minority of states other schemes for rate regulation operate. In Texas, for example, the State Board of Insurance rather than rating bureaus or individual insurers determines rates for automobile, workmen's compensation, fire, and allied lines insurance.[121] The state most well-known for its mandatory bureau membership requirement is North Carolina, where fire, auto liability, and allied lines insurers cannot do business unless they first join state-created rating bureaus.[122] Overall, about eighteen states appear to regulate at least one type of insurance through mandatory bureau membership or state-made rates. These states vary in the degree to which they permit rate deviations; some states merely limit deviations while others make them virtually impossi-

115. Casualty and Surety Rate Regulatory Bill § 13(a), NAIC PROCEEDINGS, *supra* note 100, at 406; Fire, Marine and Inland Marine Rate Regulatory Bill § 13(a), *id.* at 419.

116. Casualty and Surety Rate Regulatory Bill §§ 16-17, *id.* at 407-08; Fire, Marine and Inland Marine Rate Regulatory Bill §§ 15-16, *id.* at 420-21.

117. *See generally* materials cited in note 3 *supra*.

118. McHugh, *The Real Issue: State Versus Federal or Regulation Versus Competition?*, in INSURANCE, GOVERNMENT, AND SOCIAL POLICY 195 (S. Kimball & H. Denenberg eds. 1969).

119. Donovan, *Regulation of Insurance Under the McCarran Act*, 15 LAW & CONTEMP. PROB. 473, 485 (1950). Simultaneously, these states repealed previously existing laws that governed rate regulation. Mertz, *supra* note 96, at 166.

120. *See, e.g.*, TENN. CODE ANN. §§ 56-501 to -518, 56-601 to -616 (1968).

121. TEX. INS. CODE arts. 5.01, 5.25, 5.55 (1963).

122. N.C. GEN. STAT. §§ 58-125 to -131.9, 58-246 to -248.10 (1975). *See* note 61 *supra*.

ble.[123] Another method for regulating rates is "file and use" laws, which have been in effect over the years in at least six states[124] and permit insurers to commence using rates once they have been filed with the state insurance commissioner.[125] The commissioner, however, is entitled to suspend or disapprove the rates later if he deems it necessary.[126] Other variations of rate regulation attempted in one or two states include required filing of bureau rates only,[127] filing of rates based upon certain determinations made by the commissioner,[128] and a prohibition against bureau-set rates coupled with no requirement for filings.[129] In addition, it is worth emphasizing that a large number of states apply different types of rate regulations to different types of nonlife insurance.

(2) Other State Laws Pertaining to Competition

In addition to rating laws, other state laws, some of which are part of the insurance codes in certain states, govern industry practices and competition. A number of these laws were drafted and endorsed by the National Association of Insurance Commissioners. The model laws included the Model Act Relating to Unfair Methods of Competition and Deceptive Acts and Practices, providing for issuance by a state insurance commissioner of cease and desist orders for the following practices: misrepresentation and false advertising of policy contracts; false information and advertising generally; defamation; boycott, coercion, and intimidation; false financial statements; stock options and advisory board contracts; unfair discrimination in life insurance and annuities, and accident and health insurance; and rebates. Every state has enacted this law in some form.[130] The NAIC also recommended the enactment of legis-

123. There appears to be no provision for deviations from auto insurance rates set by the Texas Board of Insurance Commissioners, for example. On the other hand, North Carolina does permit fire insurers to deviate from rates set by the North Carolina Fire Insurance Rating Bureau, so long as deviations are uniform in their application and approved by the state insurance commissioner. N.C. GEN. STAT. § 58-131.3 (1975).

124. *See* Rose, *supra* note 18, at 704 n.177.

125. *See, e.g.*, IND. CODE § 27-1-22-4 (1975).

126. *Id.*

127. Montana apparently regulated casualty rates in this manner, but no longer does so, instead employing a nonfiling, nonbureau pricing scheme similar to that of California.

128. In Idaho, the law at one time empowered the insurance commissioner to determine periodically whether price competition within the state was reasonable. If he found that it was not, rate filings were required. The law has been repealed. Ch. 330, §§ 341-61, [1961] Idaho Laws (repealed 1969).

129. *See, e.g.*, CAL. INS. CODE §§ 1852-53.9 (West 1972). Georgia and Florida enacted similar rating laws in 1967.

130. Mertz, *supra* note 96, at 171.

lation to regulate insurance brokers, which has been done in some states.[131] A third type of legislation, drafted by the All-Industry Committee, but never recommended by the NAIC, was related to the Clayton Act, particularly sections 3, 7, and 8. Actually, two model bills were drafted, the first of which permitted interlocking directorates while the second allowed domestic insurance companies to acquire and hold stock or share capital of other insurance corporations.[132] The two model bills, enacted in various forms in over half of the states, did not deal with exclusive dealing and tying arrangements.[133] Other NAIC sponsored legislation that has been enacted in certain states includes a model law that requires accident and health insurers to file rates and policy forms and that prohibits unreasonable premiums as well as deception in or misrepresentation of policies (enacted in some form in at least eighteen states); a model bill containing similar provisions for credit life and credit accident and health insurance (enacted in some form in at least twenty-nine states); the Unauthorized Insurors Process Act (same or similar laws in force in all states); the Unauthorized Insurors False Advertising Process Act (enacted in substance in about thirteen states); the Uniform Accident and Sickness Policy Provisions Law (enacted with reasonable uniformity in every state); the NAIC Bill to Regulate Non-Profit Hospital Plans; and bills regulating group, franchise, and blanket accident and sickness insurance.[134]

Virtually every state also has antitrust laws that, in some form, prohibit monopolies and contracts, combinations, trusts, or conspiracies to monopolize or restrain trade.[135] Except in the few states where it is illegal, concerted rate making is excluded from the ambit of these antitrust laws. Generally, however, the laws do apply to other anticompetitive activities of insurers.

(3) Problems of Enforcement

The regulatory schemes currently in effect have caused problems of varying kinds that bear upon their effectiveness in protecting the consumer and in maintaining a modicum of competition among nonlife insurers. Although the problems may not be common to all the regulatory schemes mentioned in the foregoing section of

131. *Id.* at 172, 228-29.

132. *Id.* at 172-73. As noted earlier, however, the merger of insurance companies is not within the meaning of the term "business of insurance" in the McCarran Act.

133. DAY, *supra* note 4, at 31.

134. Mertz, *supra* note 96, at 173-78.

135. For a complete index of these laws see 4 TRADE REG. REP. at 35,002-08 (1976).

this Note and although to generalize is dangerous, it seems safe to say that some or all of the problems are present in the regulatory processes of most states.

The first major problem is the lack of uniformity of regulation among the states. Although the majority of state regulatory laws are derived from the NAIC/AIC model bills,[136] many of them vary slightly from the original bills. Such variations in detail, however, increase the burden of rate filings upon the industry. Not only must there be filings in almost every state, which by itself is costly, but also the filings often differ in minor yet necessary detail. Data to support rate filings,[137] for example, are necessary if a state insurance commissioner is to rule intelligently upon a rate change, and most state laws permit him, in his discretion, to control the form in which data are submitted. Texas and Massachusetts, in one or more lines of insurance, require submission of statistics in a form that differs substantially from the one used in the majority of states.[138] Even when the regulatory schemes of the states are more similar in detail, inefficiency arises by virtue of the duplication of effort among the insurance departments.[139] In addition, state boundaries may have little relation to the demographic definition of natural underwriting populations for the accurate assessment of risk and cost.[140]

A second general problem with state rate regulation is the lack of standards by which rates are set. Most states, as previously indicated, have statutes that direct themselves toward the maintenance of rates that are not excessive, inadequate, or unfairly discriminatory.[141] In many cases states have tried to define these standards,[142]

136. *See* notes 119 & 120 *supra* and accompanying text.

137. *See generally* Simon, *Statistical Agencies*, in INSURANCE, GOVERNMENT, AND SOCIAL POLICY 260, 263-78 (S. Kimball & H. Denenberg eds. 1969).

138. *Id.*

139. *See* DAY, *supra* note 4, at 67.

140. While the states with model act bills permit nationwide loss experience to be considered in determining risks, it is perfectly possible that, due to differences in regulatory schemes or regulatory judgments, citizens of different states in substantially the same circumstances will pay different premiums for the same insurance coverage.

141. Almost every state rate regulatory statute, in its statement of purposes, contains the terms "inadequate," "excessive," and "unfairly discriminatory." *See, e.g.*, MD. ANN. CODE art. 48A, § 241 (1972).

142. For example, tbe Michigan casualty rating law states:

> Rates shall not be excessive, inadequate or unfairly discriminatory. A rate shall not be held to be excessive unless the rate is unreasonably high for the insurance coverage provided and a reasonable degree of competition does not exist with respect to the classification, kind or type of risks to which the rate is applicable. A rate shall not be held to be inadequate unless the rate is unreasonably low for the insurance coverage provided and the continued use of the rate endangers the solvency of the insurer; or unless the rate is unreasonably low for the insurance provided and tbe use of the rate

but even when defined, such elusive concepts as adequacy, excessiveness, and unfair discrimination are difficult to put into practical effect. As a result, some authorities confidently have stated that insurance rates are or have been too high in certain places at certain times.[143] Other authorities have argued just as persuasively that they are or have been too low.[144] Whether the judgments of the insurance regulators in these matters have served the public well remains unanswered. Unfair discrimination has been described as existing "if allowing for practical limitations, there are premium differences that do not correspond to expected losses and average expenses or if there are expected average cost differences that are not reflected in premium differences."[145] This definition is difficult to apply because bureau-set rates are, by nature, based upon averages of the loss and expense data of many insurers, some of whose experience may vary widely from the average.[146] Further, bureau rates often are used as references by nonbureau companies, whose experience is not reflected in the bureau rates.[147] Assessments and dividends, which alter the real cost of insurance, are either not regulated or not considered in the rate approval process in many states.[148] In any case, it can be argued that the concept of unfair discrimination is essentially an ethical consideration, while actual rate regulation is in reality, and should be, based on economic considerations.[149]

With regard to excessiveness or inadequacy of rates, two further problems exist. First, excessiveness and inadequacy are usually determined by accounting for underwriting expenses and administrative expenses, and then allowing for a reasonable underwriting profit.[150] The formula does not take into consideration income derived from investing surplus funds and reserves, which is the major

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> has or will have the effect of destroying competition among insurers, creating a monopoly or causing a kind of insurance to be unavailable to a significant number of applicants who are in good faith entitled to procure such insurance through ordinary methods.

MICH. COMP. LAWS. ANN. § 500.2403(1)(d) (Supp. 1976).

143. *See* HENSLEY, *supra* note 94, at 179.

144. *See* Rose, *supra* note 18, at 726-28.

145. Williams, *Unfair Rate Discrimination in Property and Liability Insurance*, in INSURANCE, GOVERNMENT, AND SOCIAL POLICY 209, 211-12 (S. Kimball & H. Denenberg eds. 1969).

146. *Id.* at 225.

147. *Id.*

148. *Id.* at 225-26.

149. *See* Williams, *supra* note 145, at 217-24, 240.

150. *See generally* Comment, *Insurance Ratemaking Problems: Administrative Discretion, Investment Income, and Prepaid Expenses*, 16 WAYNE L. REV. 95, 101-27 (1969).

source of income for insurers.[151] Secondly, the laws of most states permit the commissioner of insurance to use statistical agencies to collect and evaluate loss and expense data.[152] It is not unusual to find rating bureaus being employed for this purpose.[153] The fact that rating bureaus have such a significant official input in the determination of the adequacy or excessiveness of the rates that they themselves, other bureaus, deviators, and independents file seems to be an undesirable conflict of interest.

Another problem, which has arisen in the past under a number of the rate regulatory laws but which has subsided considerably, involves bureau resistance to deviations, independent rate filings, and partial bureau membership. Until the mid-1960's, model act statutes in particular entitled any party aggrieved with respect to any rate filing to petition the commissioner for a hearing, at which the approval of the filing could be opposed.[154] Bureaus frequently made wholesale use of the hearings to oppose deviations, and, in some cases, appealed adverse determinations to state courts.[155] Deviations expired a year after they were granted in most states, requiring a new filing on an annual basis.[156] The sheer expense of attempting annually to justify rate deviations that might in the end go unapproved anyway were prohibitive to all but the largest and most stalwart of insurers.[157] The same kind of opposition frequently arose when bureau companies, frustrated by deviation requirements, attempted to withdraw from bureau membership insofar as it set prices for certain classes of insurance.[158] The foregoing problems, however, are now largely resolved due to statutory amendments and judicial decisions: statutory language granting aggrieved party status to rate bureaus and limiting the duration of deviations to one year has been repealed;[159] and the courts generally have sustained the right of insurers to be members or subscribers to bureaus

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151. *Id. See also* Rose, *supra* note 18, at 726-28.

152. *See, e.g.*, TENN. CODE ANN. §§ 56-513, -613(e) (1968).

153. Simons, *supra* note 137, at 263.

154. *See* notes 110 & 114 *supra* and accompanying text.

155. Rose, *supra* note 18, at 718; *see* Pugh, *Multiple Line Insurance Regulation*, in INSURANCE, GOVERNMENT, AND SOCIAL POLICY 243, 251-55 (S. Kimball & H. Denenberg eds. 1969), for a description of the concerted use of aggrieved party status on the part of single line rating bureaus to oppose the growth of broad-risk coverage, such as homeowner's policies.

156. *See* text accompanying note 112 *supra*.

157. *See* HENSLEY, *supra* note 94, at 94-95.

158. Rose, *supra* note 18, at 720-23.

159. The repeal of the one-year and aggrieved party provisions was officially endorsed in 1962-63 by the NAIC, but only after congressional pressure had been applied in the form of a Senate antitrust investigation. *See* DAY, *supra* note 4, at 29-30.

only for certain rating classes, or solely for data collection and evaluation purposes.[160]

A final problem relating to state insurance regulation involves the conduct and enforcement of the regulatory scheme itself. By virtue of being placed under state regulation, prices and practices in the insurance industry are likely to become politicized. Lobbying, public pressure, political appointments, state finance, state bureaucracy, and state legislation, all of which may be totally unrelated to the dictates of the marketplace, can affect the judgment of both the regulators and the regulated. In the words of a former New York State Insurance Commissioner:

> In most regulation, the public is only fitfully interested, and the regulator is insulated from public scrutiny by the complexity and obscurity of the regulatory process, just as the industry is insulated by the mere existence of the regulator.
>
> Left alone with each other, the regulator and his industry unconsciously find a mutual interest in ritualizing their relationship. The regulator must emphasize law and regularity, against the day he is challenged in court or denounced in public. Thus, he must look to form and detail, and may look away from the operating realities of the industry and from the expectations of the public. The industry relies on the rituals of regulation to make government behavior predictable and to keep the regulator occupied in areas where interference can be tolerated. Inevitably, both regulator and regulated come to measure their effectiveness by their impact on each other and come to live, often quite comfortably, within a closed system.[161]

The problems with state regulatory schemes are evinced by studies of individual state insurance departments. A study of the Utah Insurance Department[162] indicated that the department was underfunded and understaffed, with undertrained and underpaid employees. In fact, far more was collected by the department in purely regulatory fees, excluding taxes, than was spent on regulation. The commissioner and his staff had no direct access to an actuary or legal counsel. The regulatory authority of the department was found to be undefined to some extent, and poorly if ever implemented. In light of these observations, the study's conclusion that insurance regulation in Utah was superficial, ritualistic, and "not very effective" was understated. Another study,[163] which examined

160. *See, e.g.*, Pacific Fire Rating Bureau v. Insurance Co. of America, 83 Ariz. 369, 321 P.2d 1030 (1958). *See also* Epes, *Rate Regulation Revisited: The Views of W. Perry Epes*, in INSURANCE AND GOVERNMENT 338, 344-50 (C. Center & R. Heins eds. 1962).

161. Stewart, *Ritual and Reality in Insurance Regulation*, 1969 INS. L.J. 85.

162. Kimball & Hansen, *The Utah Insurance Commissioner: A Study of Administrative Regulation in Action*, 5 UTAH L. REV. 429 (1957), 6 UTAH L. REV. 1 (1958).

163. Franson, *The Prior-Approval System of Property and Liability Insurance Rate Regulation: A Case Study*, 1969 WIS. L. REV. 1104.

the rate regulatory branch of the New York Insurance Department, found sufficient staffing, personnel with good professional backgrounds, and adequate information storage and retrieval. Nevertheless, morale was low, and individual initiative, innovation, concern with current industry trends, and understanding of the overall function and goals of regulation only infrequently were found among the staff; evaluation, standardization, and written elaboration of procedures and policies were lacking; there was little or no enforcement of regulatory policies and procedures; and opportunities for public knowledge of and participation in the regulatory process were infrequent. A third study,[164] which dealt with the Wisconsin Insurance Department, concluded generally that the department was able to achieve success in informally settling routine, low-value, consumer complaints against insurers and agents, but that it was unable effectively to settle or mediate close legal and factual disputes. These latter two studies are somewhat disturbing because the New York and Wisconsin insurance departments are widely reputed to be two of the very best in the nation.

With regard to enforcement of laws on the part of insurance departments, a general study[165] published in 1969 concludes that although state commissioners usually are obligated to enforce insurance laws, most insurance codes do not grant commissioners broad power to suppress violations. The study points out that the weakness of insurance law enforcement is due to haphazard statutory compilation:

> The codes have not been enacted as complete and coherent systems. Rather, they constitute, for the greater part, a compilation of individual statutes, framed by different people at different times under different circumstances and influenced by different philosophies to respond to different needs and challenges in the pragmatic case-law tradition of the Anglo-American legal system. It would be vain to expect a complete and well-formulated set of enforcement tools.[166]

This language implies that the enforcement powers of insurance regulators are either inadequate or maladapted to the task of enforcement, even assuming they are used as efficiently as possible.

Certainly not all state insurance departments have problems of the same nature or magnitude as those observed in Utah. The significance of the problems found in the New York and Wisconsin studies, and the general study of enforcement, however, indicate the

164. Whitford & Kimball, *Why Process Consumer Complaints? A Case Study of the Office of the Commissioner of Insurance of Wisconsin*, 1974 WIS. L. REV. 639.

165. Pfennigstorf, *The Enforcement of Insurance Laws*, 1969 WIS. L. REV. 1026.

166. *Id.* at 1027.

naivete of assuming that the Utah regulatory scheme is a unique example of ineffectiveness. The effectiveness of insurance regulation in most states probably lies somewhere between that found in Utah and New York. Nevertheless, the inefficiency, ritualism, politicization, and lack of uniformity, standards, and adequate enforcement by the states are causes for serious concern.

Regarding the broad state antitrust and trade practices statutes, commentators, state officials, and federal officials admit that enforcement is generally nonexistent or, at best, sporadic.[167] Some states are exceptions to this rule, but they are few in number.[168] The primary reason for the shoddy enforcement of such laws is that the states lack the manpower and funds to conduct investigations, which are often extensive, and prosecute at trials, which are often protracted.[169] Additionally, broad discovery and investigative authority is often lacking.[170] Although no attempt will be made here to catalogue in detail the various state antitrust and business practices laws and the reasons why they are not enforced,[171] it seems safe to conclude that they have had, at most, a minor procompetitive effect on the insurance industry.

B. Competition Within the Regulated Nonlife Insurance Industry

Little research has been published that evaluates the competitive performance of the nonlife insurance industry under state regulatory schemes in effect since the passage of the McCarran Act. This is surely a result, at least in part, of the extreme difficulty of such a task. The data required is massive and the theoretical premises upon which conclusions might be based are disputed. Yet, some conclusions have been advanced that indicate that public demand for insurance at the lowest cost consistent with insurer reliability and solvency has not been met satisfactorily.

The major nongovernmental study of competition in the nonlife sector of the insurance industry was published in 1962.[172] The study initially found that the industry was not highly concentrated[173] over-

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167. *See* Rahl, *Toward a Worthwhile State Antitrust Policy,* 39 TEXAS L. REV. 753, 754 (1961).

168. Laws in most states, with the specific exceptions of Missouri, New York, Texas, and Wisconsin, have been described as "comatose." *Id.*

169. *See, e.g.,* Jost, *Antitrust Laws Weak in State,* The Tennessean (Nashville), Feb. 29, 1976, at B-2, cols. 5-6.

170. *Id.*

171. *See* note 135 *supra.*

172. HENSLEY, *supra* note 94.

173. *Id.* at 28.

all, and that barriers to the entry of new companies into the industry were low.[174] Another preliminary finding, based on an analysis of losses, expenses, demand, and regulated pricing practices, was that price competition, although increasing, was not prevalent.[175] Regarding property and casualty insurance lines in particular, the study stated that "rates seem to be typically established by rate bureaus that must consider the interests of all insurers concerned—the least as well as the most efficient."[176] Nonprice competition, however, was more evident throughout the industry.

The bulk of the study was an evaluation of industry performance under five criteria that were thought to be especially apt in determining whether the industry was using resources efficiently. The criteria were progressiveness, product variety, industry capacity, profitability, and selling costs.[177] Concerning progressiveness, the study concluded that "the industry has not been as progressive in developing new and better coverages, handled at less expense, as the public has a right to expect."[178] With regard in particular to accident, health, loss of income, and auto insurance, strong opposition to reform was found to exist.[179] Another important conclusion was that the industry was overly cautious and slow in responding to public needs for broad-risk policies and multiple-line insurance.[180] Lack of innovation was also a major criticism leveled at the industry under the product variety criterion. In addition, product variety in already existing lines of insurance was thought to be excessive, confusing, and of little value to consumers.[181] Under the criterion of capacity, which is the ability of the industry to supply the amount of insurance coverage demanded by the economy, the industry was found lacking.[182] It was stated that from the end of

174. *Id.* at 63-66.

175. *Id.* at 100-01.

176. *Id.* at 101.

177. What constitutes reasonable standards upon which to judge the economic performance of an industry is certainly open to debate. It can hardly be disputed, however, that progressiveness, product variety, capacity, reasonable profitability, and reasonable selling costs are qualities, ideally, for which the industry should be striving. *See id.* at 12-15.

178. *Id.* at 193.

179. *See generally id.* at 116-53.

180. The resistance to broad coverage, all-risk, and multiple lines insurance has persisted, albeit with less success. Pugh, *supra* note 155, at 243, is a more recently published discussion of the problem. Pugh states that "[d]espite some progress in recent years, there are still too many instances where the only way you can obtain multi-peril or all risk insurance is to go to foreign insurance markets free from beneficent state regulation." *Id.* He then proceeds to outline the history of insurance industry opposition to the development of multiple-peril underwriting.

181. *See* HENSLEY, *supra* note 94, at 154-56.

182. *Id.* at 156-65.

World War II "until well into 1953 the industry did not have sufficient capacity to absorb all the premiums that were offered. This was particularly true of automobile and fire insurance."[183] The regulatory requirements of the states, along with insufficient acquisition of capital on the part of the industry, were deemed responsible for the failure to meet demand. The study indicated that the capacity problem was less severe in the late 1950's, but its prediction that excess capacity would be "unlikely" during the 1960's appears, in retrospect, to have been somewhat understated.[184] Upon examining profit margins, the fourth performance criterion, the research "tentatively concluded that the average rate of return on capital at risk in the industry has frequently been 10 percentage points or more above what would seem to be necessary to obtain capital, mainly a basic interest return and an estimated return for risk."[185]

The reason for this excess was thought to be joint rate making on the part of insurers, which, as has been shown, is permitted or required in the majority of states.[186] Finally, the performance of the industry was judged on the basis of selling costs that, particularly for stock companies using independent agents as opposed to stock and mutual companies with employee sales forces, were found to be slightly higher than was deemed necessary.[187] In summary, the study indicated that industry performance was something less than satisfactory, and that considerable improvement could be achieved in a more competitive environment.

A 1962 study directed specifically at rate regulations in the automobile segment of the insurance industry[188] also reached significant conclusions about that industry's performance, which were asserted to apply to nonlife insurance generally. As in the former study, low entry barriers and economic concentration were found.[189] Contrary to the earlier study, however, evidence of the availability

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183. *Id.* at 158.

184. In an article published in 1969, Donald P. McHugh, Vice President and General Counsel of State Farm Mutual Automobile Insurance Company, stated that lack of capacity was not found to the same degree in every state, but that it was prevalent in states where insurance regulators use prior approval regulatory schemes to prevent prices from reaching proper levels. McHugh, *The Real Issue: State Versus Federal or Regulation Versus Competition?*, in INSURANCE, GOVERNMENT, AND SOCIAL POLICY 193, 199 (S. Kimball & H. Denenberg eds. 1969).

185. HENSLEY, *supra* note 94, at 195.

186. *See generally id.* at 165-79.

187. *See generally id.* at 179-90.

188. F. CRANE, AUTOMOBILE INSURANCE RATE REGULATION (1962) [hereinafter cited as CRANE].

189. *Id.* at 16-20.

of economies of scale was found inconclusive.[190] Price competition was asserted to be present and increasing, although it was admitted that competition primarily arose from direct writers and mutuals rather than the stock rating bureau companies, which wrote about half the insurance then in effect.[191] The study further revealed that "an indeterminate, but probably substantial, amount [of competition] falls in the category of secret and 'unfair' competition."[192] The two primary forms of unfair competition were thought to be intentional misclassification of risks, either to raise or lower premiums, and loss leaders, whereby insurers file low rates to attract business and later file rate increases.[193]

Concerning progressiveness, capacity, and product variety, the two studies appeared to be in general agreement.[194] On the topic of profits, the later research averred that rates were not excessive but that state rate regulation did not bring about this result;[195] regarding rate adequacy, it was found that price competition was not causally related to company failures and rate wars, but that current regulatory schemes were somewhat ineffective in preventing unfair price cutting and in encouraging product uniformity, which would permit more convenient consumer product comparisons.[196] In concluding, the study called for state regulatory reforms rather than repeal of the McCarran Act.[197]

These two studies, both more than ten years old, are pioneering works in a field that requires a great deal more investigation. The studies have been criticized[198] and undoubtedly have their faults, but they are the best independently conducted research available. They reach important conclusions with respect to competition and economic performance in the insurance industry as it was regulated in the early 1960's—conclusions that for the most part are applicable today. They show that, after ten to fifteen years under the McCarran Act, the characteristics of a competitive progressive in-

190. *Id.* at 18-19.

191. *Id.* at 41-50.

192. *Id.* at 47.

193. *Id.* at 48.

194. The study found that "[p]roduct heterogeneity is extensive, but for the most part does not represent true product rivalry and improvement." *Id.* at 118. With regard to capacity, it was asserted that inflation and growing automobile usage subsequent to World War II, along with state regulatory requirements, were responsible for an inadequate supply of insurance. *Id.* at 20-22.

195. *Id.* at 121.

196. *Id.* at 122-31.

197. *Id.* at 151-52.

198. *See, e.g.*, Brainard & Dirlam, *Antitrust, Regulation, and the Insurance Industry: A Study in Polarity*, 11 ANTITRUST BULL. 235 (1966).

dustry were less than adequately demonstrated by nonlife insurers.[199] Although there are some indications that the trend in the nonlife insurance industry in more recent years has been toward increased price competition and decreased selling costs,[200] there are also indications that progressiveness, product variety, capacity, and selling costs have continued to lag.[201]

C. Conclusion

Current state schemes for regulating insurance rates demonstrate, for the most part, the success of the nonlife insurance industry in institutionalizing the concerted setting of prices. Other state insurance laws regulating competition and business practices, which have been enacted over a period of twenty or more years, constitute an often poorly integrated patchwork of regulation that appears to have been primarily designed by the industry and NAIC to invoke the McCarran-Ferguson Act and thereby avert the impact of federal antitrust laws. The state regulatory schemes present a variety of problems that generally can be categorized as lack of uniformity, lack of standards, lack of regulatory resources, and lack of enforcement. Additionally, regulation is subject to possible political abuse and has been used by some segments of the insurance industry as a tool for oppression and prevention of change. State insurance regulation has served the public inadequately by spawning inefficiency both among the regulators and the regulated. As they apply to insurance, state antitrust and unfair business practices statutes equally have served the public inadequately. Finally, the performance of the nonlife insurance industry under state regulation has not been satisfactory.

Although insurance is "affected with the public interest"[202] and therefore requires some degree of regulation to preserve the solvency of insurers, the absence of federal antitrust jurisdiction over the

199. While the discussion in this section of the Note is not specifically addressed to ocean marine insurance, the conclusions reached are certainly applicable. *See* note 2 *supra*. Evidence emerged during a congressional investigation in 1959 indicating that regulation of marine insurance had broken down and that the industry was essentially monopolized by a small group of underwriters who were successful in keeping new entrants out of the business. SENATE COMM. ON THE JUDICIARY, THE INSURANCE INDUSTRY: AVIATION, OCEAN MARINE, AND STATE REGULATION, S. REP. No. 1834, 86th Cong., 2d Sess. 107-08 (1960).

200. *See generally* McHugh, *supra* note 184, at 201 (indicating, in 1969, that price competition in automobile insurance was highly competitive and that the control of auto rating bureaus was lessening).

201. *See generally id.* at 199 (regarding capacity); Pugh, *supra* note 155, at 256-59 (regarding progressiveness and product variety).

202. German Alliance Ins. Co. v. Lewis, 233 U.S. 389 (1914).

industry has done little to achieve that goal. At the same time, the McCarran Act has caused often burdensome and inefficient state regulation over prices and competitive practices that fails to protect the consumer's interest in obtaining adequate amounts of the types of insurance demanded at the lowest costs consistent with security. In light of the experience of the last thirty years, there can be little doubt that subjecting the insurance industry to federal antitrust law could better the plight of insurance consumers. The performance of the industry could be improved in a competitive environment, without increasing the risk that companies would default on their obligations. To this end the remainder of this Note will consist of a proposal for the attainment of such a safe but competitive environment.

IV. Proposal for Procompetitive Reform

Virtually all of the proposals for procompetitive reform of the regulatory scheme under which the insurance industry is presently governed call for either total control by the federal government[203] or improvement of state regulation.[204] A compromise approach is suggested here as being more workable. Among the justifications for a compromise proposal is that state regulatory machinery presently exists, while such machinery is absent at the federal level. The state regulatory bodies, from a practical and political perspective, would be as costly and difficult to dismantle as a federal regulatory agency would be to create.

Most state regulatory agencies and laws have been markedly more oriented toward the preservation of insurer liability and solvency than toward the stimulation of industry competition.[205] At the same time, the federal government, with its greater experience and resources, has shown itself far more adept than the states in enforcing antitrust and fair trade practices law. It therefore seems logical to permit the federal government and the governments of the states each to carry out that part of the regulation of the insurance industry for which it is presently best suited. Whatever the faults of state regulation in governing insurer reliability and solvency, there is no assurance that federal regulation would be superior in terms of uniformity, standards, enforcement, and efficiency. In light of these considerations and in the interest of rapid and uncomplicated re-

203. *See, e.g.*, HENSLEY, *supra* note 94, at 215-22.

204. *See, e.g.*, CRANE, *supra* note 188, at 151-53.

205. As has been indicated, even the rate regulatory schemes of most states have been geared to the presentation of the financial solidity of insurers rather than competition.

form, it is suggested that a single federal statute could serve the function of reserving the regulation of insurer solvency and reliability to the states, while bringing federal antitrust laws to bear on insurance industry pricing and trade practices.[206] A statute similar to the one following might be considered as a means for achieving the suggested compromise reform:

Proposed Statute

Section 1. *Declaration of Policy.*

Congress, believing that competition and fair and nondiscriminatory trade practices within the business of insurance are desirable, hereby declares that, except as provided herein, the regulation and taxation of the business of insurance is in the public interest.

Section 2. *Regulation by State Law; Applicability of Certain Federal Laws, Effective ____day of ____, 19 ____.*

(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several states that regulate and tax such business; *Provided* that after the ____ day of ____, 19 ____, the business of insurance and every person engaged therein shall not be exempt from the Sherman Act, as amended 15 U.S.C. §§ 1-7; the Clayton Act, as amended 15 U.S.C. §§ 15, 12-27, 44; the Federal Trade Commission Act, as amended 15 U.S.C. §§ 41-58, and the Robinson-Patman Anti-Discrimination Act, as amended 15 U.S.C. §§ 13, 13a, 13b, 21a.

(b) No state law that regulates or taxes the business of insurance or any person engaged therein shall be construed as invalidating, superseding, or impairing the aforementioned federal laws, or shall sanction any activity prohibited by the aforementioned federal laws.

Section 3. *Collection and Dissemination of Certain Information.*

The collection and dissemination on the part of insurers, persons engaged in the business of insurance, or independent persons or entities providing services to insurers or persons engaged in the business of insurance, solely of underwriting loss statistics and loss probability statistics, shall not constitute a violation of the Sherman Act, as amended 15 U.S.C. §§ 1-7.

206. In this respect, the proposal made here would be somewhat analogous to deregulating airline ticket prices while maintaining federal control over safety standards.

Section 4. *Applicability of National Labor Relations Act and the Fair Labor Standards Act of 1938.*

Nothing contained in this Act shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938.

Section 5. *Definitions.*

(a) As used in this Act, the term "state" includes the several states, the District of Columbia, and territories of the United States.
(b) As used in this Act, the term "regulation" excludes the regulation of the rates charged by insurance companies to their policyholders or customers.

Section 6. *Repeal of the Act of March 9, 1945 (15 U.S.C. §§ 1011-15).*

Effective on the ____ day of ____, 19 ____, the Act of March 9, 1945, codified at 15 U.S.C. §§ 1011-15, is repealed.

Section 7. *Repeal of Section 29(b) of the Merchant Marine Act of 1920 (46 U.S.C. § 885(b)).*

Effective on the ____ day of ____, 19 ____, section 29(b) of the Merchant Marine Act of 1920, codified at 46 U.S.C. § 885(b), is repealed.

The proposed statute attempts to achieve several important goals and its provisions, therefore, deserve some elaboration. The first two sections of the proposal are the heart of its state-federal allocation of insurance regulatory powers. Section 1 enunciates the policy of preserving the role of state government, subject to a proviso, in taxing and regulating insurance. The first part of section 2 expressly provides that after a certain date, which would be the same as the date in the repealers in sections 6 and 7, the four named federal laws[207] once again would apply to the insurance industry. This means that both governmental and private plaintiffs could bring actions and obtain legal and equitable remedies for violations

207. It has never heen determined whether insurance is a commodity and, therefore, whether the Rohinson-Patman Act applies to the insurance industry. *Compare* Stone & Campbell, *Insurance and the Robinson-Patman Act*, 1949 INS. L.J. 553, *with* Glassie, *Insurance and the Robinson-Patman Act: Revisited*, 1957 INS. L.J. 85. The Robinson-Patman Act is nevertheless included in the proposed statute.

of federal antitrust, antidiscrimination, and fair trade practices legislation on the part of insurance companies and their employees and agents. The second part of section 2 expressly provides for the supremacy of federal antitrust prohibitions over any type of insurance industry practices that are otherwise legal under state law. Stated conversely, section 2(b) prevents the states, in the course of their insurance regulatory functions, from legitimizing activities that would violate federal antitrust law.[208] If a state did so, federal antitrust law would preempt the state regulation.[209] With regard to the terms "insurance" and "business of insurance," which are used in sections 1 and 2 elsewhere in the statute, but are not covered by the definitional section 5, a short explanation is required. First, the term "insurance" is intended to encompass all forms of insurance, both life[210] and nonlife;[211] second, it is assumed that the term "business of insurance" would be construed by the federal courts in the same limited fashion as it has been under the McCarran Act.[212] Although the intended results likely would follow from the unelaborated use of the two terms, express definitional provisions could be inserted in section 5 if they were deemed desirable. The term "regulation" is dealt with only partially in the definitional section. Since the first two sections of the proposed statute are aimed primarily, but not exclusively, at stripping insurers and rating organizations of their anticompetitive power to fix prices, it seemed desirable to exclude expressly rate making from the scope of the term "regulation." This is not to say, however, that rate making is the only area sought to be excluded from the state regulatory bailiwick. By implication under section 2, the term "regulation" takes on a fuller meaning. In keeping with the policy of the statute, state "reg-

208. *See* note 61 *supra*.

209. The gist of § 2(b) of the proposed statute is to circumvent problems that might arise under Parker v. Brown, 317 U.S. 341 (1943). *Parker*, or the so-called primacy doctrine that it embodies, stands for the proposition that "nothing in the language of the Sherman Act or in its history . . . suggests that its purpose was to restrain a state or its officers or agents from activities directed by its legislature." *Id.* at 350-51. *See generally* Jacobs, *State Regulation and the Federal Antitrust Laws*, 25 CASE W. RES. L. REV. 221 (1975). Section 2(b) of the proposed statute seeks simply to provide direction to any court that might be tempted to conclude that state insurance regulations legitimized activity illegal under federal antitrust law. Under § 2(b), the contrary conclusion is required.

210. Since the life insurance industry is price competitive and utilizes jointly accumulated loss data without jointly setting prices, its amenability to federal antitrust laws would have only slight, yet beneficial, repercussions. *See* note 95 *supra* and accompanying text.

211. Ocean marine insurance would be covered by the proposed act. Although the ocean marine segment of the insurance industry is not discussed in detail herein, it is thought to be monopolistic and poorly regulated. *See* notes 2 & 199 *supra*.

212. *See* notes 62-75 *supra* and accompanying text.

ulation" would, or could, include regulation of policy forms, licensing of agents and salesmen, incorporation of insurance companies, specification of minimum capital or reserve levels—in short, the states would be empowered to regulate in any area except pricing insofar as it did not impinge upon the antitrust, antidiscrimination, and fair trade practices policies embodied in the four named federal statutes.

While the first two sections seek to place the insurance industry once again under the jurisdiction of federal antitrust law, section 3 expressly exempts the collection and dissemination of loss data and loss projections from the Sherman Act, implicitly providing that such activities shall not constitute illegal data dissemination. It should be noted that "solely" modifies "underwriting loss statistics and loss probability statistics," the intention being that only the data and not prices determined therefrom are within the scope of the exception. The cases in the data dissemination area appear to hold generally that the exchange of data between competitors is prohibited if it enables price stabilization and uniformity or chills the vigor of price competition.[213] Such activity, which can vary in degree, has been held to constitute either a per se or rule of reason violation of the Sherman Act.[214] Nevertheless, the nature of the risk-sharing function dictates that loss statistics and projections should be collected by and disseminated within the insurance industry.[215] Although it is not clear that a federal court would find these activities violative of the Sherman Act since the issue has never arisen, the proposed statute encourages the open exchange of the stated types of information by preventing such an eventuality. As is the case with sections 1 and 2, more precise terminology, perhaps supplemented with further definitional provisions in section 5, could be incorporated in section 3 to implement better its purpose.

The remaining sections of the proposed statute require little explanation. Section 4 is identical to section 4 of the McCarran Act[216] and fulfills the same function, which is the clarification of the insurance industry's amenability to certain federal labor legislation.

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213. *See, e.g.*, United States v. Container Corp. of America, 393 U.S. 333 (1969).

214. *Compare* American Column & Lumber Co. v. United States, 257 U.S. 377 (1921), *with* Sugar Institute, Inc. v. United States, 297 U.S. 553 (1936).

215. The law of large numbers would seem to dictate, in general, that the greater the body of loss statistics, the more accurately tbe underlying probabilities of loss can be predicted for any given policy. Therefore, a large accurate body of data will enable insurers more accurately and efficiently to determine the price of insurance. *See generally* A. MOWBRAY & R. BLANCHARD, INSURANCE 13-22 (4th ed. 1955).

216. 15 U.S.C. § 1014 (1970).

Section 5 of the proposal is the definitional section which, as previously stated, could be expanded if necessary. Section 6 repeals the McCarran-Ferguson Act, while section 7 repeals the antitrust exemption for ocean marine underwriters.[217] The effective date of both repealers would coincide with the date of the reinstated federal antitrust jurisdiction over the insurance industry in section 2.

IV. Conclusion

No claim is made that the proposal for reform or, for that matter, the analysis preceding it, is immune from attack. The subject of insurance regulation, particularly the regulation of competition, presents difficulties about which debate has raged literally for more than a hundred years. Far more thorough investigation is required. The ideals of providing insurance to consumers at the lowest possible cost while, at the same time, preserving the solvency and reliability of insurers may be to some degree irreconcilable. Both ideals, however, surely can be realized more adequately than they have been in the past. Little hazard seems to lie in the observation that insurance regulation, especially price regulation, under the McCarran-Ferguson Act largely has failed either to protect the consumer from insurance company failures or to provide him with insurance at the lowest reasonable cost. The analysis and the statutory proposal set forth here may serve at least as a stimulus for renewed efforts aimed at reform. Reform is needed, and little is to be lost by subjecting insurance to the more even-handed governance of competition.

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217. *See* notes 2, 199, & 211 *supra*.