Insurance Mergers and the Clayton Act

Section 2(b) of the McCarran-Ferguson Act is generally thought to limit the reach of Section 7 of the Clayton Act over mergers between insurance companies.[1] According to Section 2(b):

> No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any state for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance: *Provided*, that after June 30, 1948, . . . the Sherman Act, . . . the Clayton Act, and . . . the Federal Trade Commission Act, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.[2]

The meager case law holds that the proviso to Section 2(b) restricts enforcement of Section 7[3] to insurance mergers unregulated by comparable state antitrust laws.[4] While the proviso explicitly mentions the Clayton Act, the body of Section 2(b) could also be read to hamper

1. "Section 2(b) of the McCarran Act, however, restricts the application of Section 7 where the merger involves two insurance companies. To the extent that state laws regulate such mergers, the McCarran Act exempts them from the effects of the Clayton Act." Note, *Application of Federal Antitrust Laws to the Insurance Industry*, 46 MINN. L. REV. 1088, 1101 (1962). This is one of the leading commentaries. *See also* SUBCOMM. OF THE PUBLIC REGULATION OF THE BUSINESS OF INSURANCE COMM., ABA SEC. INSURANCE, NEGLIGENCE AND COMPENSATION LAW, MERGER OF INSURANCE COMPANIES 71 (1966) [hereinafter cited as ABA INSURANCE MERGERS]; Brainard and Dirlam, *Antitrust Regulation and the Insurance Industry: A Study in Polarity*, 11 ANTITRUST BULL. 235 (1966); Stern, *The McCarran Act Twenty Years After*, 1966 INS. L.J. 605; *see* p. 1409 *infra*.

2. 15 U.S.C. § 1012(b) (1964).

3. 15 U.S.C. § 18 (1964). While § 7 is the chief federal weapon against anticompetitive mergers, § 1 of the Sherman Act may also be used. *See* United States v. First Nat'l Bank & Trust Co., 376 U.S. 665 (1964) (civil suit against merger of two banks). The Sherman Act, along with the Federal Trade Commission Act, should apply to insurance mergers for the same reasons that § 7 should. *Cf.* United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 346-48 (1963).

4. Only two cases have considered this question. In Maryland Cas. Co. v. American Gen. Ins. Co., 1964 CCH Trade Cas. ¶ 71,188 (D.D.C. 1964), a private § 7 suit brought against merging insurers from two states, the court based its jurisdiction on the following grounds:

> No regulation of the proposed acquisition of control of Maryland or its agencies can be adequate or effective because of territorial limitations of Texas and Maryland regulation. Texas and Maryland statutes do not provide for adequate or effective regulation of the proposed acquisition of control of Maryland or its agencies and there is no such regulation thereunder as precludes this suit under the antitrust laws.

Id. at 79,721.

In United States v. Chicago Title & Trust Co., 242 F. Supp. 56 (N.D. Ill. 1965), legislative and territorial constraints provided the grounds for federal antitrust jurisdiction over a merger between Illinois and Missouri insurers. While Missouri had an anti-merger law, Illinois insurance laws regulated only the rate-making and solvency aspects of mergers. In addition to the Illinois insurer's immunity from the Missouri law, the merger's effects in ten other states underscored the territorial problem.

Section 7 enforcement. Section 7 would thus be unable to "invalidate, impair, or supersede" any state statute regulating the "business of insurance." The Supreme Court's latest reading of Section 2(b),[5] however, should result in a salutary broadening of the scope of the Clayton Act to include all insurance mergers.[6]

I. Congressional Policy Toward Insurance Mergers

The only interpretation of the McCarran-Ferguson Act which harmonizes its historical background, underlying objectives and various sections shows that Congress intended no antitrust exemption for insurance mergers.[7] The insurance industry, which requested the legislation, expressly refused to ask for such an antitrust exemption.[8] Indeed, many proponents of the bill emphasized that it was intended to promote competition.[9] But rate-making in concert, a peculiarity of insurance deemed essential to proper risk distribution,[10] constituted

5. SEC v. National Securities, Inc., 393 U.S. 453 (1969).

6. Future federal challenges to anticompetitive insurance mergers seem likely.

> [T]he Federal Trade Commission has taken active steps to stem the rising tide of insurance company mergers. . . . The Commission is conducting an in-depth study to determine the market structure and how merger activity affects the competitive climate of the automobile insurance industry. . . . Recently, this Division [of Mergers of the Federal Trade Commission] has instituted several investigations of mergers involving insurance companies. Justification for inquiry into any substantial merger affecting the insurance industry does exist, and it is safe to conclude that during the remainder of the year 1969, Division activity will be greatly increased.

Reffkin, "Mergers"—Conglomerates Purchasing Insurance Companies—Insurance Companies Purchasing Other Insurance Companies, May 26, 1969 (address before Annual Convention of New Jersey Association of Independent Insurance Agents) 15-17.

The Antitrust Division of the Department of Justice is "taking a hard look at some of these insurance company mergers." McLaren, Address before Fifth Annual Meeting of the American Insurance Assoc. May 21, 1969, 8-9. The Justice Department recently warned that it would probably try to block any merger between two insurance companies if they are similar in size to the 200 largest manufacturing corporations. N.Y. Times, June 7, 1969, at 1, col. 8.

7. "Congress never intended to grant federal immunity to mergers involving insurance companies based on the action or inaction of the states." Reffkin, *supra* note 6, at 13.

8. When the insurance industry proposed the legislation, it said that "No attempt has been made to deal with the subjects of joint stock ownership and interlocking directorates which will have further study." 90 CONG. REC. A4406 (1944) (Joint Statement of Chairman of Exec. Comm. and Chairman of Subcomm. on Fed. Legislation of Nat'l. Ass'n. Ins. Commrs.). "It will be noted that in the draft of the proposed text of legislation no provision has been made with reference to stock acquisitions and interlocking directorates. This is not because these matters have been overlooked." *Id.* at A4408 (conclusion to memorandum explaining proposed legislation).

9. *See* 90 CONG. REC. A3975-77 (Report of the Subcomm. on Federal Legislation, Nat'l. Ass'n. Ins. Commrs.); S. REP. No. 1834, 86th Cong., 2d Sess. 3 (1960); Hansen, *Insurance Competition and the Antitrust Laws*, 1957 INS. L.J. 669, 671. This type of exemption had also previously been said to encourage competition. H.R. REP. No. 873, 78th Cong. 1st Sess. 9 (1943).

Moreover, Section 3(b) of the McCarran-Ferguson Act expressly makes the antitrust laws applicable to acts of boycott, coercion and intimidation. 15 U.S.C. § 1013(b) (1964).

10. Free competition in rate-setting had been found to tempt insurers to charge less than what was needed to cover future losses, leading to insolvencies. To provide a

price-fixing[11] and therefore required an antitrust exemption. The original draft of Section 2(b), prepared by insurance companies and state insurance officials, enumerated only cooperative rating and closely related matters as warranting an antitrust exemption.[12] As a result, the debates on the exemption concerned rate-making, not mergers.[13]

When compared to previous bills and other sections of the Act itself, the antitrust exemption in Section 2(b) does not seem to deal with mergers. An earlier bill,[14] passed by the House of Representatives,[15] declared that "nothing contained in the [antitrust laws] shall be construed to apply to the business of insurance or *acts in the conduct of such business*."[16] This wording apparently put almost all insurance company activities—including mergers—beyond the antitrust laws.[17] Several legislators complained about the breadth of this bill's language,[18] and their complaints may have led to the Senate's killing the bill.[19] Similarly, the McCarran-Ferguson Act at some points refers broadly to "the business of insurance, and every person engaged therein"[20] and to "the business of insurance or acts in the conduct

broader, more exact base for predicting losses and charging rates, insurers pooled statistics. Rating bureaus, membership in which was often mandatory, collected this information and promulgated supposedly reasonable rates. *See* H.R. REP. No. 873, *supra* note 9, at 7-9.

11. United States v. South-Eastern Underwriters Ass'n., 322 U.S. 533 (1944).

12. 90 CONG. REC. A3977, A4405-A4406 (1944) (Report of the Subcomm. on Federal Legislation, National Ass'n. of Ins. Commrs., Recommendation Four) (§4[b] of the proposed legislation).

13. *See* 91 CONG. REC. 478-88, 1441-44, 1447-88 (1945). *Cf.* SEC v. National Securities, Inc., 393 U.S. at 458. Remarks in the debates about the Clayton Act therefore are not applicable to the purported exemption for mergers.

While the final wording of the exemption did not enumerate every activity exempted, it was understood to apply only to those anticompetitive insurance practices inherently necessary to the insurance function. 91 CONG. REC. A1625 (reprint of article by Senator O'Mahoney, *The New Federal Insurance Law*). *See id.* at 489, 1443 (remarks of Senator O'Mahoney). There was no itemization in order to allow new developments in insurance underwriting to fall within the exemption. *See* 91 CONG. REC. 485 (remarks of Senator Radcliff).

Thus, the exemption is quite narrow. Wiley, *Pups, Plants and Package Policies—Or the Insurance Antitrust Exemption Reexamined*, 6 VILL. L. REV. 281, 349-50 (1961); Note, *Regulation of Insurance Advertising Practices: A Jurisdictional Inquiry*, 67 YALE L.J. 452, 453 n.4 (1958). It has even been suggested that cost factors in insurance reflecting non-risk elements and not contributing to the "goal of actuarial creditability, should not enjoy exemption from the antitrust laws." Note, *State Supervision over Insurance Rate-Making Combinations Under the McCarran Act*, 60 YALE L.J. 160, 167 (1951).

14. S. 3270, H.R. 1369, H.R. 1370, 78th Cong., 1st Sess. (1943).

15. 90 CONG. REC. 6565 (1944).

16. (Emphasis added).

17. *Hearing Before a Subcomm. of the Senate Comm. on the Judiciary on S.1362*, 78th Cong., 1st Sess. 25 (1943) (testimony of Attorney General Biddle).

18. *See, e.g.*, 90 CONG. REC. 6417 (1944) (remarks of Congressman Voorhis).

19. 90 CONG. REC. 8054 (1944).

20. 15 U.S.C. § 1012(a) (1964).

thereof."[21] In contrast, the proviso restricts its antitrust exemption to only the "business of insurance."[22] The body of Section 2(b) likewise speaks of laws designed to regulate only the "business of insurance."

Section 3(a) of the McCarran-Ferguson Act immunized for three years "the business of insurance or acts in the conduct thereof" from several federal laws.[23] During that time, Congress gave the states the chance to pass regulatory legislation concerning rate-making and other insurance activities.[24] For mergers, though, this moratorium was designed to allow further study of the need for an antitrust exemption.[25] The exemption expired after three years, and Congress enacted no new merger legislation. While every state accepted the moratorium's invitation to pass laws regulating insurance rate-making, only a few enacted legislation concerning anticompetitive insurance mergers.[26] This legislative inertia has been attributed to the states' tacit recognition that Congress never intended to exempt insurance mergers from Section 7.[27]

Even if legislative intent were not so clear, the requirement that an antitrust exemption must be explicit should resolve any doubt against the existence of an exemption for mergers.[28] Moreover,

21. "Until June 30, 1948, . . . the Sherman Act, and . . . the Clayton Act, and . . . the Federal Trade Commission Act, and . . . the Robinson-Patman Anti-discrimination Act, shall not apply to the business of insurance or acts in the conduct thereof." 15 U.S.C. § 1013(a) (1964).

22. "The statute did not purport to make the States supreme in regulating all the activities of insurance *companies;* its language refers not to the persons or companies who are subject to state regulation, but to laws 'regulating the *business* of insurance'." SEC v. National Securities, Inc., 393 U.S. at 459.

Furthermore, in contrast to the negative language of the defeated bill, the proviso is phrased affirmatively so that the antitrust laws "shall be applicable to the business of insurance. . . ." By using positive wording, Congress may have expressed more forcefully the reach of the antitrust laws over insurance companies. *See* United States v. Chicago Title & Trust Co., 242 F. Supp. at 65.

23. *See* note 21 *supra.*

24. S. REP. No. 20, 79th Cong., 1st Sess. 2 (1945); 91 CONG. REC. 1089 (1945) (remarks of Congressman Anderson). *See also* Berdon, *Insurance—The Regulation Phase,* 22 CONN. B.J. 149, 153 (1948).

25. 90 CONG. REC. A4408 (1944) (conclusion to memorandum of Insurance Commissioners explaining proposed legislation).

26. *See* ABA INSURANCE MERGERS at 80; Berdon, *supra* note 24, at 158-59; Note, *Application of Federal Antitrust Laws to the Insurance Industry, supra* note 1, at 1101. As of 1966, only nineteen states had such laws purporting to regulate anticompetitive insurance mergers.

27. Berdon, *supra* note 24, at 158-59. But soon after Congress passed the McCarran-Ferguson Act, certain commentators assumed that it also covered the antitrust aspects of insurance mergers. *See, e.g.,* Naujoks, *Regulation of the Insurance Business and Public Law No. 15, 79th Congress, First Session,* 30 MARQ. L. REV. 77, 96 (1946); Orfield, *Improving State Regulation of Insurance,* 32 MINN. L. REV. 219, 229-30 (1948); Sawyer, *A Program Under Public Law 15,* 1946 INS. L.J. 72, 75.

28. United States v. Philadelphia National Bank, 374 U.S. at 348; California v. Federal Power Commission, 369 U.S. 482, 485 (1961). Since, as a result of the *South-Eastern Underwriters* decision, the federal antitrust laws apply to insurance companies, the proviso to Section 2(b) cannot be read to yield a negative inference that they apply to *only*

even explicit exemptions are strictly construed.[29] The importance of maintaining a competitive economy militates against an implied antitrust exemption based on ambiguous legislative intent.[30] Consequently, any antitrust exemption contained in Section 2(b) should be interpreted narrowly.[31]

II. The Need for Expanding the Scope of Section 7

Despite Congressional intent and the principle of narrow construction, courts and federal officials alike have read Section 2(b) to inhibit Section 7's effectiveness against anticompetitive insurance mergers.[32]

"the business of insurance," narrowly defined. The better reading is that federal antitrust laws reach all activities of insurance companies, but those activities in "the business of insurance" are exempt insofar as the states regulate them.

29. *See* ABA INSURANCE MERGERS at 70; Michels, *Insurance—The Case Against Broad Exemptions From the Antitrust Laws*, 20 FED. B.J. 66, 73 (1960).

30. The Supreme Court applied Section 7 to bank mergers despite a widely assumed exemption. United States v. Philadelphia Nat'l Bank, 374 U.S. 321 (1963). "Of course, our construction of the amended Section 7 is not foreclosed because, after the passage of the amendment, some members of the Congress, and for a time the Justice Department, voiced the view that bank mergers were still beyond the reach of the Section." *Id.* at 348. The bank merger case thus closely resembles the insurance merger situation.

31. The courts, though, have sometimes strayed from a narrow construction of the insurance antitrust exemption. In Prudential Ins. Co. v. Benjamin, 328 U.S. 408 (1946) (state power to tax out-of-state insurer), the Supreme Court said that the purpose of the McCarran-Ferguson Act was "broadly to give support to existing and future state systems for regulating and taxing the business of insurance." Later courts accented the adverb "broadly" and sometimes overlooked the phrase "business of insurance." Thus the antitrust exemption became more extensive. *See* Transnational Ins. Co. v. Rosenlund, 261 F. Supp. 12 (D. Ore. 1966); California League of Independent Ins. Producers v. Aetna Cas. and Sur. Co., 175 F. Supp. 857 (N.D. Cal. 1959); Professional and Businessman's Life Ins. Co. v. Bankers Life Co., 163 F. Supp. 274 (D. Mont. 1958).

32. *See* note 4 *supra*. After FTC v. National Cas. Co., 357 U.S. 560 (1958), the Department of Justice and the Federal Trade Commission applied the standard contained in that opinion to insurance mergers, with poor results. "[W]e recently considered a proposed merger (which had been reported in the press) between a large property insurance company and a life insurance company. Since the pertinent State insurance statutes contain so-called Little Clayton Acts, we concluded that the Clayton Act was not applicable to the merger." Letter from Victor R. Hansen, Assistant Attorney General in charge of the Antitrust Division, to Senator Joseph O'Mahoney, Dec. 12, 1958, quoted in *Hearings Before Subcomm. on Antitrust and Monopoly of Senate Comm. on the Judiciary Pursuant to S. Res. 57*, 86th Cong., 1st Sess., pt. 2, at 930-31 (1960).

Though various shortcomings in state regulation of insurance mergers have been interpreted as allowing federal antitrust regulation, such an interpretation still presupposes that Section 2(b) theoretically restricts the scope of Section 7. *See* S. REP. No. 1834, *supra* note 9; Hansen, *Merger of Insurance Companies and Antitrust Law*, 1958 INS. L.J. 782. In 1967, for example, the present Chairman of the FTC wrote that federal antitrust "jurisdiction over [insurance acquisitions] results from the absence, inadequacy or impossibility of state regulation." Dixon, *Federal Antitrust Laws and the Insurance Industry*, PROCEEDINGS OF THE LEGAL SECTION OF THE AMERICAN LIFE CONVENTION 246 (1967).

Earlier this year, an FTC attorney said insurance mergers are subject to § 7 because of the inability of the states to regulate them properly. Reffkin, *supra* note 6. The current Assistant Attorney General in charge of the Antitrust Division thinks only a "majority of insurance company mergers are subject to the federal antitrust laws." McLaren, *supra* note 6, at 8.

According to their interpretation of the proviso, mergers between insurance and non-insurance firms fall within Section 7 because one of the merging firms is outside the "business of insurance."[33] On the other hand, a merger between two insurance companies supposedly triggers the exemption. As soon as the proviso comes into play, only mergers involving insurers from different states are considered fair game for Section 7.[34] Following this view, the federal government has gone to court only once to stop an anticompetitive insurance merger.[35] Effective state antitrust regulation of intrastate mergers allegedly would preclude federal antitrust regulation altogether. But no state has ever brought an antitrust suit against an insurance merger.[36]

In this permissive climate, some segments of the insurance industry recently have shown a clear trend toward concentration.[37] Along with growing concentration, tight insurance markets have developed.[38] These telltale anticompetitive signs coincide with an unprecedented and increasing number of insurance mergers.[39] Although the insurance

33. Hansen, *supra* note 32, at 785. The Justice Department had no hesitation in challenging the merger of Hartford Fire Insurance Company and International Telephone and Telegraph. *See* Wall Street Journal, June 24, 1969, at 3, col. 1.

Similarly, non-insurance companies, including holding companies, which acquire insurance subsidiaries probably are also exposed to Section 7. But such exposure has been questioned. Stern, *The Future of State Regulation*, ABA Sec. Insurance, Negligence and Compensation Law, Proceedings, 221, 223-24 (1968).

34. Under existing theory, federal antitrust jurisdiction results primarily from the territorial limitation of state enforcement. Consequently, there have been suggestions that the federal law would apply if the anticompetitive impact of the merger were felt in other states. But the only two cases involved merging insurers from different states.

35. United States v. Chicago Title & Trust Co., 242 F. Supp. 56 (N.D. Ill. 1965).

36. *See* Reffkin, *supra* note 6, at 5; S. Rep. No. 1834, *supra* note 9, at 216.

37. Dixon, *supra* note 32, at 249. The trend is readily seen in fire and casualty, where "concentration is slight but on the rise. In life and health, concentration is high but apparently on the decline." ABA Insurance Mergers, *supra* note 1, at 90.

In New York, the state with the largest amount of insurance written, the top twenty-five fire and casualty companies "showed a small but steady trend in the direction of concentration" from 62% to 68% of the market during 1950-1966. The trend also appeared among automobile insurers, going from 63% in 1950 to 76.5% in 1966. Rep. of the Supt. of Ins. to N.Y. Legislature, 17-19 (1968). Moreover, the number of casualty, surety, fire and marine companies licensed in New York decreased from 466 in 1948 to 423 in 1958. Am. Agency Bull., July, 1963, *Two Important Trends: Mergers and Packaging* 22, 23.

38. Rep. of N.Y. Special Comm. on Holding Cos., Feb. 15, 1968, at 13.

39. No fewer than 282 acquisitions have been consummated or approved between the years 1960 and 1968 involving insurance companies, with an indeterminate number of companies having conducted discussions seeking similar results. In 1968 alone there were over 100 announcements of pending marriages where both companies involved insurers. There were approximately 27 announcements of engagements between insurance companies and non-insurers.

Reffkin, *supra* note 6, at 4-5. *See also* ABA Insurance Mergers, *supra* note 1, at 3-4; Amos, *The Merger Movement in the Insurance Industry*, 19 Fed. Ins. Couns. Q. 11 (1969); Bernstein, *A Regulator's View of Corporate Mergers*, *id.* at 17, 18. One commentator noted that "[o]ne can hardly leaf through a current insurance journal without noting one or more stories of amalgamations being considered, launched, or completed." He

industry is still characterized by a large number of competitors with small market shares, national market share and concentration statistics may be deceptively low. Frequently, one fleet organization runs several insurance companies, thus reducing the total number of truly independent firms.[40] In addition, many insurers are only regional, so that national statistics may mask the true degree of concentration in relevant geographic markets.[41] In such an economic setting, therefore, vigorous enforcement of Section 7 might accomplish one of its major purposes: to stop incipient monopoly.[42]

In fact, the peculiarities of the insurance industry call for strict surveillance of potentially anticompetitive mergers.[43] From the outset, the inherent need for rate-making in concert limits insurance competition. Thus, if an insurer subscribing to a rating bureau merges with a non-bureau company, a rare source of price competition disappears.[44] Mergers also may eliminate some of the small independent insurers which are often the first to experiment with new types of

expects "[e]ven greater amalgamation activity in the future." Williams, *Report on "The Insurance Merger Handbook"*, ABA SEC. INSURANCE NEGLIGENCE AND COMPENSATION LAW, PROCEEDINGS, 405 (1965). A Senate study some years ago had anticipated "this accelerated merger tempo." S. REP. No. 1834, *supra* note 9, at 225-26.

Many insurers are also forming holding companies and acquiring insurance subsidiaries. STANDARD AND POOR'S INDUSTRIAL SURVEYS—INSURANCE, Vol. 137, No. 6, § 1, Feb. 6, 1969, at 12; *id.* BASIC ANALYSIS, Nov. 7, 1968, at 18.

40. R. HENSLEY, COMPETITION, REGULATION AND THE PUBLIC INTEREST IN NONLIFE INSURANCE 197 (1962); Dixon, *supra* note 9, at 247.

41. Each state's own requirements for a company to sell insurance tend to discourage small insurance companies from branching out beyond their home states.

42. The Supreme Court has consistently underscored the necessity of arresting monopoly in its incipiency. In amending Section 7,

> Congress sought to preserve competition among many small businesses by arresting a trend toward concentration in its incipiency before that trend developed to the point that a market was left in the grip of a few big companies. Thus, where concentration is gaining momentum in a market, we must be alert to carry out Congress' intent to protect against ever increasing concentration through mergers.
>
> . . . Congress feared that a market marked at the same time by both a continuous decline in the number of small businesses and a large number of mergers would slowly but inevitably gravitate from a market of many small competitors to one dominated by one or a few giants, and competition would thereby be destroyed.

United States v. Von's Grocery Co., 384 U.S. 270, 277-78 (1966). *See* United States v. Pabst Brewing Co., 384 U.S. 546, 552 (1966); United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 367 (1963); Brown Shoe Co. v. United States, 370 U.S. 294, 317-18 (1962).

Only a few years ago, the Superintendent of Insurance of New York defended the antitrust exemption for insurance mergers by noting that "the [Pabst] case involved 'an industry marked by a steady trend toward economic concentration', a situation *not* analogous to that in the insurance industry." [Emphasis added.] Stern, *supra* note 1, at 614. His statement, whether it was accurate even then, certainly is not true today. Indeed, "[w]hen the tendency toward concentration is heightened by mergers and acquisitions there is greater cause for alarm." McHugh, *The Congress Looks At Insurance*, 8 FED. INS. COUNS. Q. (No. 4) 5, 15 (1958).

43. In this respect, insurance is much like banking. It is a highly regulated financial industry essential to the national economy. United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533, 539-42 (1944). As a result, competition becomes more crucial. *Cf.* United States v. Philadelphia National Bank, 374 U.S. 321, 372 (1963).

44. S. REP. No. 1834, *supra* note 32, at 225.

policies.[45] More important, insurance companies underwrite only those risks regarded as satisfactory.[46] An insurer's ability to deny coverage reduces the number of product sources. In a tight insurance market, coverage for undesirable risks often becomes unavailable at any price.

III. The Antitrust Exemption after *SEC v. National Securities*

Although past interpretation has assumed that Section 2(b) protects mergers, the proviso insulates only the "business of insurance." But the word "business" is susceptible of several definitions. Sometimes it means an enterprise, and when considered as a group of like enterprises, an industry. Hence, an insurance company is an insurance "business" and all insurance companies together form an industry called the "business of insurance." These enterprise-industry definitions comprise the semi-articulated premise of present antitrust enforcement.[47] In other contexts, however, "business" is the particular commercial *activity* conducted by an enterprise or industry. Consequently, the insuring activities of an insurance company are another possible definition of the "business of insurance."

In *SEC v. National Securities, Inc.*,[48] the Supreme Court attempted for the first time to define explicitly the term "business of insurance." The SEC contended that two merging Arizona insurance companies violated its anti-fraud rules.[49] Arizona has a statute that regulates in-

45. Hedges, *Improving Property and Casualty Insurance Coverage*, 15 LAW & CONTEMP. PROB. 353, 355 (1950).

46. Some commentators have made the serious mistake of putting insurance into the same class as utilities. *See* Hale and Hale, *Competition or Control I: The Chaos in the Cases*, 106 U. PA. L. REV. 641 (1958); Hale and Hale, *Competition or Control IV: Application of Antitrust Laws to Regulated Industries*, 111 U. PA. L. REV. 46 (1962). But utilities and common carriers must serve all comers at reasonable rates. Such regulated industries are said to trade their market discretion for exemption from the antitrust laws. The mistake in classifying insurance as a utility probably stems from an attempt to rationalize an assumed antitrust exemption. *See* Hale and Hale, *Mergers in Regulated Industries*, 59 NW. U.L. REV. 49, 55 (1964).

47. FTC attorney Reffkin asks "why should the federal government express concern about an industry whose 'business' Congress felt could be adequately regulated on a local level by the states?", but then proceeds to offer the conventional reasons for Section 7 jurisdiction: defects in the quality and extent of state regulation. Reffkin, *supra* note 6, at 4 ff. *See* Hansen, *supra* note 32 at 782; Mertz, *The First Twenty Years—A Case-Law Commentary on Insurance Regulation Under the Commerce Clause*, ABA SEC. INSURANCE, NEGLIGENCE AND COMPENSATION LAW, PROCEEDINGS, 153, 178, 180 (1964).

48. 393 U.S. 453 (1969).

49. Defendant, which owned a controlling interest in one insurer, acquired control of the board of directors of another insurance company. After proposing the merger, defendant sought the approval of the second company's stockholders. In soliciting these proxies, it allegedly misrepresented the obligations of the surviving company, thereby violating Rule 10(b)5. The Securities and Exchange Commission wanted to enjoin the merger. Since the merger was accomplished despite its disapproval, the Commission now claimed the right to "unwind" the merger in order to return to the status quo ante.

surance company stock proxies,[50] and another that permits an insurance merger if security and service for existing policyholders will be adequate.[51] The Court held that, despite state approval of the merger, federal jurisdiction existed to unwind it. Inasmuch as no antitrust violation was alleged, Justice Marshall's opinion focused on the body of Section 2(b), rather than the proviso. The Court construed "business of insurance" as a term of art denoting the "relationship between insurer and insured, the type of policy which could be issued," and a policy's "reliability, interpretation and enforcement."[52] According to the Court, this definition includes rate-setting, selling and advertising of policies, and licensing of companies and their agents.[53] Those activities of insurance companies which affect their status as reliable insurers are also part of the "business of insurance."[54] All other activities—such as soliciting stock proxies—are outside the "business of insurance" and subject to federal regulation.[55] Arizona's law controlling insurance company stock proxies therefore does not regulate the "business of insurance."[56] Moreover, although Arizona's statute regulating solvency and service requirements is a type encompassed by Section 2(b), the federal remedy does not "invalidate, impair, or supersede" it. There is no impairment primarily because the federal interest in protecting investors is distinct from any state interest in protecting policyholders of the merging companies.[57]

The definition of "business of insurance" provided by *National*

50. ARIZ. REV. STAT. § 20-731 (Supp. 1969).
51. ARIZ. REV. STAT. § 20-731(B)(3) (Supp. 1969).
52. 393 U.S. at 460.
53. *Id.*
54. "Undoubtedly, other activities of insurance companies relate so closely to their status as reliable insurers that they too must be placed in the same class." *Id.*
55. "Insurance companies may do many things which are subject to paramount federal regulation; only when they are engaged in the business of insurance does the Statute [the McCarran-Ferguson Act] apply." *Id.* at 459-60.
56. Arizona is concerning itself with a markedly different set of problems. It is attempting to regulate not the "insurance" relationship, but the relationship between a stockholder and the company in which he owns stock. This is not insurance regulation, but securities regulation. . . . The crucial point is that here the State has focused its attention on stockholder protection; it is not attempting to secure the interests of those purchasing insurance policies.

Id. at 460.
57. The Federal Government is attempting to protect security holders from fraudulent misrepresentations; Arizona, insofar as its activities are protected by the McCarran-Ferguson Act from the normal operations of the Supremacy Clause, is attempting to protect the interests of the policyholders. . . . The paramount federal interest in protecting shareholders is in this situation perfectly compatible with the paramount state interest in protecting policyholders. And the remedy the Commission seeks does not affect a matter predominantly of concern to policyholders alone; the merger is at least as important to those owning the companies' stock as it is those holding their policies.

Id. at 463.

Securities belies the assumption—seemingly taken for granted—that Section 2(b) limits the applicability of Section 7 to insurance mergers. Although the Court construed only the body of Section 2(b), there is no reason why its definition of "business of insurance" should not apply to the same phrase in the proviso. According to this definition, mergers in themselves are surely not part of the "business of insurance."[58] Merging—like soliciting proxies,[59] selling securities,[60] or settling creditor claims in bankruptcy[61]—reflects an insurer's corporate nature rather than its particular industry.[62]

Of course, a merger can affect an insurance company's "status as a reliable insurer" and for that reason might be included in the "business of insurance." The financial condition of one partner may impair the other company's ability to pay claims and service policyholders.[63] But because merger is a non-insurance activity, it should be classified as part of the "business of insurance" only insofar as the precise effects sought to be regulated jeopardize the reliability or enforcement of the merging companies' insurance policies.[64] A merger can have many

58. Courts reading Section 2(b) this way scrutinize the particular activity at issue. *Cf.* Hill v. National Auto Glass Co., 293 F. Supp. 295 (N.D. Cal. 1968), where the court remarked that "while the settlement of claims by the payment of money could certainly be considered to reasonably fall within the general meaning of 'business of insurance,' it does not seem to this court that the alleged activity involved here, namely, securing for particular glass dealers the sales and installation jobs required by Allstate claimants, is a part of the 'business of insurance' as that term is normally understood." *Id.* at 296. *See* notes 59-61 *infra.*

59. In United States v. Meade, 179 F. Supp. 868 (S.D. Ind. 1960), the federal securities antifraud rules were imposed on a company organized for purposes other than selling insurance. "[E]ngaging in the solicitation for, sale of, and transportation of the capital stock of the Agency Corporation cannot be said to be the business of insurance within the meaning of the McCarran Act. . . ." *Id.* at 876.

60. The Court itself has held that an insurance company selling a variable annuity must register it under the Securities Exchange Act of 1933, despite both the insurance aspects of the annuity and the state regulation. SEC v. United Benefit Life Ins. Co., 387 U.S. 202 (1967); SEC v. Variable Annuity Life Ins. Co. of America, 359 U.S. 65 (1959). Selling a variable annuity is not the same as selling "insurance." *See* United States v. Meade, 179 F. Supp. 868 (S.D. Ind. 1960).

61. Although an amendment to the McCarran-Ferguson Act was at one time thought necessary to bring insurance company liquidations under federal law, Note, *Insurance Liquidations: A Proposed Amendment to the McCarran-Ferguson Act*, 66 YALE L.J. 1072 (1957), a state court has forced creditors of a bankrupt insurance company to settle claims according to federally prescribed priorities on the theory that an insurer in receivership no longer transacts "business." Langdeau v. United States, 363 S.W.2d 327 (Tex. Civ. App. 1962).

62. A former New York Superintendent of Insurance differentiated between "corporate activities, those which an insurance company shares with most other kinds of corporations, and insurance activities, those as to which the business of insurance is the central fact." Wikler, *Insurance and the Antitrust Laws. A State Outlook*, 1963 INS. L.J. 534, 536.

63. For the same reason, merger with a non-insurer, or indeed any action potentially endangering an insurance company's accumulated funds and reserves, should be included in the "business of insurance."

64. The distinction which *National Securities* draws between a primary insurance activity, like rate-making, and a non-insurance activity, like merger, which may have secondary effects on an insurer's reliability, is crucial. It weakens any attempt to dis-

consequences, and only some of them endanger the standing of the merging companies as reliable insurers. As a result, mergers take on a chameleon-like quality: whether they should be considered part of the "business of insurance" depends on the type of law being enforced against them. For the purposes of a law regulating practices which affect reliability of the merging companies, a merger is properly regarded as part of the "business of insurance." But a merger's anticompetitive effects pose no threat to the solvency and reliability of the merging insurers. Accordingly, so far as Section 7 is concerned, no reason exists for regarding the merger as part of the "business of insurance." Since the proviso to Section 2(b) applies only to the "business of insurance," it grants no federal antitrust exemption whatsoever to insurance mergers.

While an anticompetitive insurance merger is outside the "business of insurance" with respect to federal antitrust laws, state regulation[65] of it under the body of Section 2(b) might still be thought to restrict the scope of Section 7. State laws which proscribe insurance mergers having anticompetitive effects,[66] for instance, might be viewed as enacted "for the purpose of regulating the business of insurance."[67] Admittedly, such statutes test illegality by the merger's effects upon product competition. Since selling policies is the "business of insurance," these state laws may therefore appear to be indirectly aimed at that "business." Like Section 7, however, such laws are actually de-

tinguish proxy solicitation from the actual merger itself in an antitrust case. To be sure, the SEC

> did not ask the trial court to pass directly upon a merger which the State Director of Insurance had approved. No question of the legality or illegality of the merger, standing alone, was raised. The gravamen of the complaint was the misrepresentation, not the merger. The merger became relevant only insofar as it was necessary to attack it in order to undo the harm caused by the alleged deception.

SEC v. National Securities, Inc., 393 U.S. at 462. But because a merger may have some effects on the buying and selling of policies does not mean that it therefore should be automatically thought of as part of the "business of insurance." Only for its effects on the reliability of the merging companies should it be so classified.

Moreover, "the case for characterizing a transaction or series of transactions as insurance is weakened if there is no need to impose insurance regulation." Denenberg, *The Legal Definition of Insurance*, in ESSAYS IN THE THEORY OF RISK AND INSURANCE 210, 226 (J. Hammond ed. 1968). *See generally* Kimball, *The Purpose of Insurance Regulation: A Preliminary Inquiry in the Theory of Insurance Law*, 45 MINN. L. REV. 471 (1961).

65. But these state laws may not be regulation enough to satisfy the McCarran-Ferguson Act. They are aimed at interstate effects of mergers when such regulation was meant to be left with the federal government. *See* Hamilton Life Ins. Co. v. Republic Nat'l Life Ins. Co., 291 F. Supp. 225, 232 (S.D.N.Y. 1968).

66. *See, e.g.*, N.Y. INS. LAW § 67 (McKinney 1964); CONN. GEN. STAT. § 38-37 (1969).

67. Simply because a law applies only to insurance companies does not make it a law regulating the "business of insurance." *National Securities* itself described an application of a state statute only to insurance companies as a "mere matter of form" of no importance. 393 U.S. at 460. *See also* Langdeau v. United States, 363 S.W.2d 327, 331 (Tex. Civ. App. 1962).

signed to protect market and societal values which apply to insurance companies as well as other firms.[68] The market tests formulated by the courts in applying Section 7 are only indicia of a merger's ultimate consequences,[69] including its social and political overtones.[70] In reality, the states are attempting to cope not with the "insurance relationship"[71] but with the problems of industrial organization.[72]

State laws requiring merging insurers to maintain solvency and service adequate for their policyholders do regulate the "business of insurance."[73] These state statutes, however, are no more impaired by enforcement of Section 7 than by enforcement of the SEC's antifraud rules. Just as the federal government has an important, distinct interest in protecting investors,[74] it has an equally unique and essential interest in preserving competition and inhibiting industrial concentration in the national economy.[75] Merely because a merger meets a

68. Pressing in upon the insurance enterprise from without are all the goals of society at large. For the most part the insurance business would work equally well whether these objectives were implemented or not. This is so far true that regulatory officials do not always recognize clearly that national economic policy, or other general economic policy, has any relationship to supervision . . . . These general societal goals are pervasive demands which have as much validity within the insurance institution as they have anywhere else . . . . There is no reason to isolate insurance from the rest of society.

Kimball, *supra* note 64, at 500-01, 506. *See also* Sawyer, *supra* note 27, at 76.

69. *See* United States v. Continental Can Co., 378 U.S. 441, 458 (1964). *Cf.* FTC v. Procter & Gamble Co., 386 U.S. 568, 578 (1967).

70. *See* Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics*, 74 HARV. L. REV. 226, 236, 247-49, 304-05 (1960). The weighing of conflicting economic and social interests is unavoidable. *See also* Turner, *Conglomerate Mergers and Section 7 of the Clayton Act*, 78 HARV. L. REV. 1313, 1394-95 (1965). The Court itself early recognized a merger's threat to non-economic values. Brown Shoe Co. v. United States, 370 U.S. 294, 315-16 (1962).

71. Regulation of the "insurance relationship" means control of an insurer's activities so its policyholders get the benefits of their contracts. "The McCarran-Ferguson Act was an attempt . . . to assure that the activities of insurance companies in dealing with their policyholders would remain subject to state regulation." SEC v. National Securities, Inc., 393 U.S. 453, 459 (1969). But the Act gave no new or additional regulatory powers to the states. H.R. REP. No. 143, 79th Cong., 1st Sess. 3 (1945).

72. United States v. Chicago Title & Trust Co., 242 F. Supp. 56 (N.D. Ill. 1965), implicitly recognized this distinction when it called "legislation on other insurance or antitrust matters" insufficient. *Id.* at 60. *Cf.* Wikler, *Insurance and the Antitrust Laws. A State Outlook*, *supra* note 62, at 536. But such fine analysis has been criticized. Stern, *The McCarran Act Twenty Years After*, *supra* note 1, at 613.

Nevertheless, courts look closely at the type of law involved. In Hamilton Life Ins. Co. v. Republic Nat'l Life Ins. Co., 408 F.2d 606 (2d Cir. 1969), the Court of Appeals called it "quite plain that arbitration statutes, including those of Texas and New York are not statutes regulating the business of insurance, but statutes regulating the method of handling contract disputes generally." *Id.* at 611. Furthermore, the Texas arbitration statute, according to the District Court's opinion affirmed on appeal, "is a codification of an old common-law rule, whose purpose was not to regulate the insurance business but rather to preserve the jurisdiction of the courts." 291 F. Supp. 225, 232 (S.D.N.Y. 1968). *See* Langdeau v. United States, 363 S.W.2d 327, 331-32 (Tex. Civ. App. 1962).

73. SEC v. National Securities, Inc., 393 U.S. 453, 462 (1969).

74. Indeed, for some years the courts have applied the federal securities laws to insurance companies. *See, e.g.*, Zachman v. Erwin, 186 F. Supp. 691 (S.D. Tex. 1960); United States v. Meade, 179 F. Supp. 868, 876 (S.D. Ind. 1960).

75. *See* note 42 *supra*.

state's solvency standards should not preclude the federal government from safeguarding separate national interests. In applying federal laws regulating maritime accidents,[76] trademarks,[77] and mail fraud[78] to insurance companies, courts have found no impairment of state regulation of the "business of insurance." *National Securities* itself expressly rejected the argument that Section 2(b) bars "any attempt to interfere with a merger approved by state insurance officials," as an "overly broad restriction on federal power."[79]

Moreover, state statutes regulating mergers to protect existing policyholders merely permit certain insurers to merge.[80] No command ordering the merger issues from the state.[81] However, even if a state would order an anticompetitive merger to avert the insolvency of one of the merging companies,[82] the merger should not be exempt from Section 7. Such a merger situation would seem to produce a direct conflict between the state interest in preventing insurance insolvencies and the federal interest in preserving competition. But the conflict would be minimized by recognition of an enlarged "failing company" defense for insurance mergers. The widespread public effects of insurance failures, compared to ordinary business bankruptcies, justify the use of a relaxed "failing company" standard in judging insurance mergers.[83] Despite recent weakening of the vitality of this defense,[84]

76. Maryland Cas. Co. v. Cushing, 347 U.S. 409 (1954).

77. In Sears, Roebuck & Co. v. All States Life Ins. Co., 246 F.2d 161 (5th Cir. 1957), state approval of an insurer's name did not bar a federal cause of action by another company with a similar name. "[T]here is nothing in the McCarran Act that limits the right of the owner of a trade or service name to seek redress in the federal courts merely because the approval of the name of the infringing insurance company is part of the duties of the state board." *Id.* at 172.

78. United States v. Sylvanus, 192 F.2d 96 (7th Cir.), *cert. denied*, 342 U.S. 943 (1951).

79. 393 U.S. at 463.

80. "Arizona has not commanded something which the Federal Government seeks to prohibit. It has permitted respondents to consummate the merger; it did not order them to do so." SEC v. National Securities, Inc., 393 U.S. 453, 463 (1969).

81. This situation is not comparable to that in Parker v. Brown, 317 U.S. 341 (1943), where state legislation set up an anticompetitive agricultural program. "[A] state does not give immunity to those who violate [a federal antitrust law] by authorizing them to violate it, or by declaring that their action is lawful." *Id.* at 351-52. But in North Little Rock Trans. Co. v. Cas. Recip. Exch., 85 F. Supp. 961 (E.D. Ark. 1949), *aff'd*, 181 F.2d 174 (8th Cir.), *cert. denied* 340 U.S. 823 (1950), a district court in holding that fixed automobile liability insurance rates did not violate the federal antitrust laws said that those laws are "not violated by acts *authorized* and *regulated* by state statute." 85 F. Supp. at 964 (emphasis added).

82. At present, there is no such state law and the probabilities of unwilling insurance companies being *forced* to merge is unlikely.

83. *See* Note, *Application of Federal Antitrust Laws to the Insurance Industry*, *supra* note 1, at 1103; *see* Dixon, *supra* note 32 at 249 n.20; McHugh, *Insurance and Antitrust Laws. An Industry Outlook-Casualty Insurance*, 1963 INS. L.J. 547, 552.

84. *See* Citizen Publishing v. United States, 394 U.S. 131 (1969); *see* Bock, *Failing 'Failing' Company: Justification for Mergers*, N.Y.L.J., June 25, 1969, at 1, cols. 4-5.

the Supreme Court has shown a sensitivity to it in the related field of banking.[85]

IV. Conclusion

Since no state has ever attacked an anticompetitive insurance merger, federal antitrust law seems to be the only means of halting the current trend of insurance concentration. Preserving competition in the insurance sector of the economy would be in the long-range interest of insurers,[86] as well as the public. But the precise scope of Section 7 over insurance mergers has never been authoritatively determined. By activating the proviso without discussion, previous lower court decisions begged the question of whether mergers are the "business of insurance." After *National Securities*, however, no court should construe any part of Section 2(b) to restrict federal antitrust challenges to insurance mergers. Certainly state insurance laws may coexist with Section 7, and their concurrent jurisdiction could mean that effective enforcement of them might make the exercise of federal power unnecessary. In no way, however, does a state's antitrust policy condition the existence of that federal power.

85. In the *Philadelphia National Bank* case, the Court wrote:

> Section 7 does not mandate cutthroat competition in the banking industry, and does not exclude defenses based on dangers to liquidity or solvency, if to avert them a merger is necessary. . . . Thus, arguably, the so-called failing company defense . . . might have somewhat larger contours as applied to bank mergers because of the greater public impact of a bank failure compared with ordinary business failures.

374 U.S. at 371-72, 372 n.46.

Some commentators have thought that the investment company defense should also apply to insurance mergers. Hansen, *supra* note 32, at 787; Note, *Application of Federal Antitrust Laws to the Insurance Industry*, *supra* note 1, at 1102-03. But this very characteristic of insurance companies—substantial investment in other companies—supplies an additional reason for halting concentration in insurance. A highly concentrated insurance industry may lead to concentration in other fields. *Cf.* Address by McLaren, *supra* note 6, at 9.

86. Already, tight insurance markets have prompted some states to set up assigned risk pools for automobile and fire insurance. Under such pooling arrangements, insurance companies are forced to cover all risks.

> If, in the future, the insurance business lives more by the rules of the rest of the economy, and the public believes it is doing so, the public will tend to treat the insurance business more like other businesses. If the insurance business does otherwise, the public will tend to treat it more like an extension of government—demanding fuller public accountability for its actions and wider public representation in its revenue raising, and resting indifferent when its functions are absorbed by government.

Stewart, "The End of Isolationism in Insurance Regulation," Remarks at Fifth Annual Meeting of American Insurance Ass'n, May 21, 1969. Consequently, for insurance companies to refrain from claiming a special antitrust exemption for mergers might be in their self-interest. Such action could perhaps forestall more onerous regulation tending to convert insurance companies into quasi-utilities, or even more drastic, full-scale government assumption of the insuring process.