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Debate on State versus Federal Regulation of Insurance Continues: *American General Insurance Co. v. FTC*, 359 F. Supp. 887 (S.D. Tex. 1973)

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Casenote

Debate on State Versus Federal Regulation of Insurance Continues

American General Insurance Co. v. FTC, 359 F. Supp. 887 (S.D. Tex. 1973)

For over a century there has been a continuing controversy concerning state versus federal regulation of insurance. Since the passage of the McCarran-Ferguson Act[1] (hereinafter the "McCarran Act"), the primary responsibility for regulation has been with the states.[2] However, the decision in *American General Insurance Co. v. FTC*[3] once again raises the issue of federal regulation of certain areas of the insurance trade. In *American General*, the court held that the language of the McCarran Act limiting the application of thte Clayton Act[4] to those situations where the business of insurance is not regulated by state law did not deprive the Federal Trade Commission ("FTC") of jurisdiction to challenge a merger between two insurance companies. There were two grounds for this holding. First, the court concluded that state regulation would be impossible because of the extraterritorial impact

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1. 15 U.S.C. § 1012 (1958) [hereinafter cited as McCarran Act]:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
>
> (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, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

2. This is the policy of Congress as set forth at 15 U.S.C. § 1011 (1958):

> Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

3. 359 F. Supp. 887 (S.D. Tex. 1973).
4. 15 U.S.C. § 18 *et seq.* (1970).

of such a merger.[5] Further, the court noted that under the McCarran Act, states are exempted from federal statutes only if they regulate the "business of insurance."[6] The court concluded that since merger activity was not part of the "business of insurance," it was not subject to state regulation.[7]

The case involved a merger agreement between American General Insurance Company, an insurance holding company with its principal place of business in Houston, Texas, and Fidelity and Deposit Company of Maryland, an insurance company with its principal place of business in Baltimore, Maryland. The FTC filed a complaint alleging that the effect of the merger would be substantially to lessen competition or to create a monopoly in violation of section 7 of the Clayton Act.[8] After a determination by the full commission that the FTC was not preempted by the McCarran Act from challenging the merger,[9] the insurance companies filed suit in district court seeking an injunction to halt further action by the FTC. The court dismissed the complaint for failure to exhaust administrative remedies,[10] but in so doing considered the merits of the case.

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5. 359 F. Supp. at 895.
6. *Id.* at 896.
7. *Id.* at 897.
8. 15 U.S.C. § 18 (1970):

   > No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly. . . . .

9. The administrative law judge of the FTC had held that there was adequate state regulation of the merger and granted the insurance companies' motion for summary decision and dismissal of the complaint. The decision was appealed to the full commission and the determination of the administrative law judge was vacated.
10. The plaintiff insurance companies contended that the commission's denial of their motion for summary decision was a final ruling under the Administrative Procedure Act, 5 U.S.C. § 704 (1964). The FTC responded that the denial of the motion for summary decision was only an interlocutory order and not a "final ruling." Further, the FTC argued that in any event, the proper forum for review of proceedings initiated under § 7 of the Clayton Act, 15 U.S.C. § 18 (1970), was the court of appeals. The court rejected plaintiffs' contention and held that it had no jurisdiction under the Administrative Procedure Act to review the commission's action because the denial of the motion for summary decision was neither an action made reviewable by statute nor a final agency action for which there was no adequate remedy in a court.

This casenote will be limited to a discussion of the court's holding that the McCarran Act did not deprive the FTC of jurisdiction to challenge insurance company mergers as violations of the Clayton Act.

The problem faced by the court in *American General* had its beginnings in 1868 when the United States Supreme Court held in *Paul v. Virginia*[11] that a state statute requiring insurance companies to be licensed before they could carry on business within the state was constitutional. The court reasoned that the issuance of an insurance policy was not a transaction of commerce and insurance contracts were not articles of commerce.[12] During the more than 75 years that this view prevailed, the states became dominant in the field of insurance regulation.

In 1944 the Supreme Court held in *United States v. South-Eastern Underwriters Association*[13] that the business of insurance constituted interstate commerce and that the Sherman Act was applicable to interstate insurance transactions.[14] The period immediately following the *South-Eastern* decision was one of uncertainty for both the insurance companies and the states. The states feared that taxes imposed on insurance contracts written within their borders might be considered an unconstitutional burden on interstate commerce.[15] Because of the uncertainty surrounding the ability of the states to tax, the insurance companies were refusing to pay their taxes or paying them under protest.[16] Many believed that the scheme of state regulation which had emerged between the

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Plaintiffs, relying on Leedom v. Kyne, 358 U.S. 184 (1958), further argued that administrative remedies need not be exhausted in situations where an agency clearly is exceeding its jurisdiction. The court rejected plaintiffs' argument and concluded that *Kyne* provided an exception to the exhaustion rule only in those situations where the assertion of jurisdiction by the agency is in "flagrant disregard of their statutory authority . . . ." 359 F. Supp. at 892, or where plaintiffs lack an adequate remedy at law. *See* K. Davis, Administrative Law Text §§ 20.01, 20.02, 20.03, 20.05 (3d ed. 1972), where the author indicates that the area of exhaustion is unsettled and that the only "rule" in the area is that "*sometimes* exhaustion is required and *sometimes not.*" *Id.* § 20.02 at 384 (emphasis original). Davis suggests that the proper way to decide questions of exhaustion would be to examine (1) the extent of possible injury, (2) the doubt or clarity about administrative jurisdiction and (3) the possibility of specialized administrative understanding. *Id.* § 20.10 at 194.

11. 75 U.S. (8 Wall.) 168 (1868).
12. *Id.* at 183.
13. 322 U.S. 533 (1944).
14. *Id.* at 560.
15. 91 Cong. Rec. 1087 (1945) (remarks of Representative Hancock).
16. *Id.*

Paul decision and the *South-Eastern* decision had been severely shaken.[17]

The Congressional response to this uncertainty was the passage of the McCarran Act. In order to encourage the "continued regulation and taxation by the several States of the business of insurance,"[18] the following provisions were enacted:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
>
> (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, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance; *Provided,* That after [a moratorium period], the . . . Sherman Act, and . . . 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.[19]

Thus, in the absence of specific federal legislation, the states were free to regulate and tax the business of insurance except that certain federal legislation (including the Clayton Act) would, after a moratorium period,[20] be "applicable to the *business of insurance* to the extent that such business is not *regulated by State law.*"[21]

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17. Donovan, *Regulation of Insurance Under the McCarran Act,* 15 LAW & CONTEMP. PROB. 473, 476 (1950).
18. 15 U.S.C. § 1011 (1958).
19. 15 U.S.C. § 1012 (1958).
20. 15 U.S.C. § 1013 (1958) provides in part:
    > (a) Until June 30, 1948, the . . . Sherman Act, . . . the Clayton Act, . . . the Federal Trade Commission Act, and . . . the Robinson-Patman Anti-Discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.
    > (b) Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

    This provision was included to exempt the states, for a period of approximately 3 years, from the provisions of the named legislation. This was necessary to give the states time to enact, if they so desired, legislation which might otherwise conflict with the suspended laws. It should be noted that § 1013(b) ensures the continued application of the Sherman Act to agreements to or acts of boycott, coercion or intimidation. *See* 91 CONG. REC. 1443 (1945) (remarks of Senators McCarran and Ferguson).
21. 15 U.S.C. § 1012(b) (1958) (emphasis added). This entire scheme of regulation was challenged in Prudential Ins. Co. v. Benjamin, 328 U.S. 408 (1946) as being inconsistent with the commerce clause,

I.

The resolution of the issue of what constitutes state "regulation" sufficient to preempt federal action provided the first basis for the holding in *American General.*[22] The plaintiffs urged that the regulation of merger activity was the province of the states and that only in those instances where there was *no* attempt to pass regulatory legislation would the FTC have jurisdiction to challenge mergers.[23] Plaintiffs argued that the merger between American General and Fidelity and Deposit was regulated in two respects: first, by the antitrust laws of the principal places of business of the merging companies[24] and second, by the licensing requirements of each of the states where the resulting company would be engaged in business.[25] The court rejected the argument that the

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but was upheld by the Court. *See* B. SCHWARTZ, CONSTITUTIONAL LAW § 71 (1972).

22. What must be done to constitute "regulation" is not precisely clear. In the Senate debate on the McCarran Act, the following exchange took place:

> Mr. MURDOCK: . . . Does the Senator take the position that the states could absolutely repeal all their insurance laws and still be regulating insurance?
>
> Mr. PEPPER: Well, if they repeal the laws and had no regulation, of course, that would not be regulation.

91 CONG. REC. 1481 (1945) (remarks of Senators Murdock and Pepper). Thus, at a minimum, states must *legislate.* The Supreme Court in FTC v. National Cas. Co., 357 U.S. 560 (1958), assumed that "there is some difference . . . between 'legislation' and 'regulation,' . . . ." *Id.* at 565. The Court concluded that the petitioner in that case had not argued that the statutory provisions involved were a "mere pretense" and therefore could not question the effectiveness of the statutes. More recently, the sixth circuit in Ohio AFL-CIO v. Insurance Rating Bd., 451 F.2d 1178 (6th Cir. 1971), refused to look at the quality of state regulation. It had been alleged that state rating regulations were not effective. The court found no support for the contention that there should be an inquiry into the effectiveness of the state's enforcement of its regulations. The Supreme Court denied certiorari, 409 U.S. 917 (1972), with Justice Douglas arguing in dissent that the question of whether or not the regulation was a "mere pretense" should be decided. This sequence of events has led one author to conclude that the courts will not make "a qualitative evaluation regarding a state's regulating activities even if it is alleged that the regulatory activity is a pretense, ..." Sfikas, *The Quality of State Regulation Necessary to Invoke the Insurance Exemption to the Antitrust Laws,* 1973 INS. L.J. 305, 310.

23. 359 F. Supp. at 893.

24. *Id.* at 894. The merger between the two companies was approved by the insurance authorities of both Maryland and Texas, but the court made no reference to the specific statutes under which the merger was approved.

25. *Id.*

states had regulated the merger concluding that a state has no ability to regulate beyond its borders, and, because of this disability, could be expected to take a parochial view of a proposed merger.[26] In the words of the court, a state would not "examine a merger in terms of [its] national effect."[27] The implication of the court's reasoning appears to be that state regulation of merger activity is not possible.[28]

The court's conclusion that a state is unable to regulate merger activity is premised on the inability of states to regulate extraterritorially.[29] To support its contention, the court in *American General* placed primary reliance on *FTC v. Travelers Health Association*.[30] In that case an insurance company organized in Nebraska and licensed to do business only in Nebraska and Virginia sold insurance policies through the mails in all states. The FTC charged the company with employing deceptive advertising practices in violation of the Federal Trade Commission Act.[31] A Nebraska statute prohibited deceptive trade practices in Nebraska or in any other state.[32] The court of appeals determined that this state statute was sufficient "regulation" to preclude federal legisla-

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26. *Id.*
27. *Id.*
28. *See* Note, 46 MINN. L. REV. 1088, 1097 (1962).
29. The statements of Senator O'Mahoney illustrate the Congressional intent on this point:

    > [T]here is not a line or sentence in the proposed act, as I have read it, which would delegate to any State the power to legislate in the field of interstate and foreign commerce. State regulation must be for the State and not for the United States.

    and

    > Nothing in the proposed law would authorize a State to try to regulate for other States, or authorize any private group or association to regulate in the field of interstate commerce.

    91 CONG. REC. 1483 (1945) (remarks of Senator O'Mahoney). *See also* FTC v. Travelers Health Ass'n, 362 U.S. 293, 300 (1960); Ohio AFL-CIO v. Insurance Rating Bd., 451 F.2d 1178, 1184 (6th Cir. 1971); United States v. Chicago Title & Trust Co., 242 F. Supp. 56, 72 (N.D. Ill. 1965).
30. 362 U.S. 293 (1960), *rev'g* 262 F.2d 241 (8th Cir. 1959), *remanded*, 298 F.2d 820 (8th Cir. 1962).
31. 15 U.S.C. § 45 (1970).
32. > No person shall engage in this state in unfair methods of competition or in unfair or deceptive acts and practices in the conduct of the business of insurance. No person domiciled in or a resident of this state shall engage in unfair methods of competition or in unfair or deceptive acts and practices in the conduct of the business of insurance in any other state, territory, possession, province, country, or district.

    Ch. 191, § 2 [1957] Neb. Laws 666-67.

tive control under the McCarran Act.[33] The Supreme Court reversed and held that "the state regulation which Congress provided should operate to displace [the Federal Trade Commission Act] means regulation by the State *in which the deception is practiced and has its impact.*[34]

On remand, the eighth circuit interpreted the Supreme Court's holding to mean that the state in which the deception was practiced and had its impact would have to "regulate" the practice through legislation "capable of being enforced through the exercise of its own powers."[35] Because 48 of the 50 states would have to rely on the statutes, instrumentalities and processes of Nebraska in order to exercise legal compulsion, the court held that the activities involved were not "regulated by State law" within the meaning of the McCarran Act.[36]

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33. 262 F.2d 242 (8th Cir. 1959).
34. 362 U.S. 293, 298-99 (1960) (emphasis added). The Court stated the same definition another way when it concluded that Congress, when it used the term "regulated," meant "only regulation by the State where the business activities have their operative force." *Id.* at 301-02.
35. 298 F.2d 820, 823 (1962).
36. *Id.* at 824-25. The concept of state enforcement of its *own* legislative provisions through the exercise of its *own* judicial powers as established by the Supreme Court and the eighth circuit in *Travelers Health* is essential in determining whether a state "regulates" in situations where two or more states are affected by an activity. There are two conditions precedent to "regulation": first, a state must have legislation, and second, it must be able to enforce this legislation through its own powers. Assuming that a state has a regulatory scheme, the next question is whether it can *enforce* the regulation. This is not a question of jurisdiction, which under modern statutes would be obtainable in most situations. The ultimate issue is that of post-judgment enforcement, and was illustrated by the eighth circuit:

> [I]n forty-eight of the states, Travelers Health Association is without any license, agency relationships, commercial accounts, or other direct presence of person or property, upon which the state can auxiliarly lay hands in enforcement compulsion. If its orders, decrees and judgments are to be enforceable, the state must seek the aid of the statutes, instrumentalities and processes of another state.

Id. at 824-25. A case presenting this problem in the context of the regulation of merger activity is United States v. Chicago Title & Trust Co., 242 F. Supp. 56 (N.D. Ill. 1965). There Illinois and Missouri were the domiciliary states of two insurance companies seeking to merge. The court found that Missouri's statutes did not "cover Chicago Title's absentee acts, *nor could they be enforced* against Chicago Title," *id.* at 71-72 (emphasis added), and that Illinois' antitrust statutes were not applicable to the business of insurance. In short, Illinois had no legislation and Missouri had legislation but no means of enforcing it.

The court in *American General* concluded that "the extraterritoriality rationale of Travlers applies with equal force to federal antitrust regulation under the Clayton Act."[37] However, the application of the *Travelers Health* rationale to merger activity is questionable for two reasons. First, the rule in that case was applied to the easy factual situation. There, the test of whether there was "regulation" was whether the state *in which the activity was practiced and had its impact* could regulate the particular activity.[38] Due to the nature of the activity involved in *Travelers Health* (mail order advertising which was alleged to be deceptive), it was "practiced" and had its "impact" in a single state—the state where the advertising was received. This was not the case in *American General.* The activity to be regulated (merger) is theoretically "practiced" in the two domiciliary states (Maryland and Texas), but its impact also occured in 48 other states. Since the "practice" and "impact" are split between two or more states, the considerations governing whether there has been "regulation" will be different from the situation where the regulated activity is practiced and has its impact in the same state.[39]

Moreover, the applicability of the *Travelers Health* rationale to the facts of *American General* is questionable because unlike the situation in *Travelers Health,* the company formed as a result of the merger was licensed to do business in all 50 states.[40] Therefore, if the effect of the merger spread across state lines, the states affected would have the power to enforce through judicial compulsion their own regulatory legislation concerned with the effect of merger activity. The plaintiffs in *American General* argued that this was one form of state regulation.[41] The problem with this type of regulation is that it comes after the fact. The activity to be regulated is the merger, and it would have taken place before states which grant the resulting company a license to do business pass judgment. Therefore, effective regulation is most likely to occur only in those states that have initial control over a proposed merger. These are the only states which could refuse to allow the companies to merge. A refusal by the domiciliary states to ap-

37. 359 F. Supp. at 895.
38. 362 U.S. at 298-99.
39. The problems presented by the multi-state impact of a merger might be eliminated by analyzing the situation in terms of the relevant area affected. It might be argued that due to the extensive regulation of the business of insurance by the individual states, the affected area extends only to the borders of the state. The impact would then occur within a single state by definition.
40. 359 F. Supp. at 894.
41. *Id.*

prove a merger application would appear to meet the requirements of *Travelers Health* since the regulation could be enforced through the exercise of the states' own powers, and the activity is practiced and has an impact in those states. However, the impact is also felt in other states, and the question which ultimately must be answered is whether regulation by the states initially approving the merger is adequate regulation insofar as other affected states are concerned.

Traditionally, the purposes of insurance regulation have been largely parochial in nature,[42] and it appears that the regulation of merger activity is not an exception.[43] However, if the domiciliary states feel that competition would be lessened and deny the application to protect their own citizens, the citizens of other states would be indirect beneficiaries. Such a theory of regulation would force the citizens of one state to rely on the regulations of another state for protection—a result which the Supreme Court found objectionable in *Travelers Health*.[44]

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42. *See* Kimball, *The Purpose of Insurance Regulation: A Preliminary Inquiry into the Theory of Insurance Law*, 45 MINN. L. REV. 471 1961). Kimball, while recognizing that the relationships of insurance companies with the outside world will have some effect on their regulation, sees the primary role of insurance regulation as that of insuring the successful operation of the company itself. The premise underlying this theory is that the policyholder will be protected so long as the "solidity" of the company is protected.
43. A limited perspective with respect to merger activity is evidenced by § 3(d)(1) of the Model Insurance Holding Company System Regulatory Act which provides for the approval of a merger unless, *inter alia*, "the effect of the merger or other acquisition of control would be to substantially lessen competition in insurance *in this State* or tend to create a monopoly therein. . . ." *Proceedings*, 1969 NAT'L ASS'N OF INS. COMM'RS 738, 744 (vol. 2). This factor was noted by the court in *American General*. 359 F. Supp. at 894 n.5.
44. 362 U.S. at 296-97, 298-99. This point was made explicitly by Judge Vogel who dissented in the circuit court opinion. 262 F.2d at 245. In considering the case on remand, the eighth circuit found enforcement relying on comity between states insufficient "regulation" under the McCarran Act. The court explained that it had contemplated a situation in which states having regulatory legislation would cooperate with states which were affected by an activity but had no means of judicial compulsion:

    > [I]f Travelers Health Association sent improper soliciting material into a state where it was not licensed, the insurance department of such state would bring the matter to the attention of the Nebraska Director and he would take appropriate steps to deal with the situation in accordance with his official responsibility.

    298 F.2d at 822. The court went on to note that the Supreme Court "made it clear that this . . . [did] not constitute the type of control to which the McCarran-Ferguson Act requires the Federal Trade Commission Act to yield." *Id.*

The analytical problems in applying the rationale of *Travelers Health* to merger activity are compounded by an inconsistency between the way states choose to regulate the business of insurance in practice, and the theoretical premise implicit in applying Clayton Act concepts to the business of insurance. The chief regulatory approach taken by the states is to treat insurance as a "regulated industry" subject to rate regulation[45] and a system of contract approval.[46] The assumption underlying this type of state regulation and the assumptions underlying the Clayton Act are in apparent conflict. On one hand, the states recognize that the business of insurance is primarily non-competitive and therefore subject it to regulation, the purpose being to force the insurance industry to operate *as if* it were competitive.[47] On the other hand, the implication in applying the Clayton Act to the business of insurance is that the insurance industry is no different than any other industry and must operate in a manner consistent with the ideal of a free and open market place.

The relevant inquiry under the McCarran Act is whether or not a particular activity is "regulated" by state law. The "regulated industry" approach to insurance regulation does not regulate competition in the same way as the Clayton Act does, but arguably, the same purposes are ultimately achieved. Recent decisions indicate that courts are hesitant to pierce the veil of state regulatory schemes in order to question the quality or effectiveness of the regulation.[48] At least one court, however, has rejected the "regulated industry" approach as an alternative to the application of Clayton Act concepts.[49] If this traditional type of state regula-

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45. *See* Kimball & Boyce, *The Adequacy of State Insurance Rate Regulation: The McCarran-Ferguson Act in Historical Perspective*, 56 MICH. L. REV. 545 (1958); STATE OF NEW YORK INSURANCE DEPARTMENT, THE PUBLIC INTEREST NOW IN PROPERTY AND LIABILITY INSURANCE REGULATION pt. IV (1969).
46. Kimball & Pfennigstorf, *Legislative and Judicial Control of the Terms of Insurance Contracts: A Comparative Study of American and European Practice*, 39 IND. L.J. 675 (1964).
47. *See* Nankin Hosp. v. Michigan Hosp. Serv., 361 F. Supp. 1199 (E.D. Mich. 1973); Travelers Ins. Co. v. Blue Cross, 361 F. Supp. 774 (W.D. Pa. 1972) (Blue Cross was not monopolistic because "it not only lacks control over the rate-making effects normally incident to lawful competition, but is without power to establish its own rates. . . ." *Id.* at 780).
48. *See* note 22 and accompanying text *supra*.
49. In United States v. Chicago Title & Trust Co., 242 F. Supp. 56 (N.D. Ill. 1965), the acquisition of the stock of a Missouri insurance company by an Illinois insurance company was challenged as a violation of section 7 of the Clayton Act. It was argued that Missouri had a "public utility" approach to rate regulation and therefore achieved

tion is rejected as inadequate, the inquiry in the area of state regulation of merger activity will most likely focus on the extraterritorial problems of regulation which occur when Clayton Act concepts are applied.[50] This could lead to a re-evaluation of state regulatory schemes and possibly bring about a major change in the theory of state regulation of the business of insurance.[51]

II.

The second basis for the court's decision in *American General* was that merger activity was not the "business of insurance" as contemplated by the McCarran Act.[52] In construing the term "business of insurance," the court relied solely on *SEC v. National Securities, Inc.*,[53] which involved a proposed merger between two insurance companies. The SEC alleged violations of the Securities Exchange Act[54] and sought a dissolution of the merger because of certain omissions and misrepresentations made to the stockholders of one of the companies when the merger was submitted for their approval. The district court denied relief[55] and the ninth

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the same objective as would have been the case under the antitrust statutes. The court rejected this approach saying:

> The instant case is one where the states have not [acted comparably to Section 7] even though in one respect their "public utility approach" may accomplish the same end as antitrust regulation. The Federal Government has decided competition is healthy economics and that intent is not necessarily satisfied because one of its ends is achieved by another means.

Id. at 71. *Contra*, Travelers Ins. Co. v. Blue Cross, 361 F. Supp. 774 (W.D. Pa. 1972), *aff'd*, 481 F.2d 80 (3d Cir. 1973), *cert. denied*, 42 U.S.L.W. 3352 (U.S. Dec. 10, 1973) ("Congress . . . recognized the fact that the salutary effects of competition may be accomplished by regulation as well." *Id.* at 781).

50. *See* notes 41-43 and accompanying text *supra*. One author has suggested an approach where the regulation of the competitive aspects of the business of insurance is left to the federal government as a possible solution. McHugh, *The Real Issue: State Versus Federal or Regulation Versus Competition?* in INSURANCE, GOVERNMENT, AND SOCIAL POLICY 193, 203 (S. Kimball & H. Denenberg eds. 1969) [hereinafter cited as McHugh].
51. *See* McHugh, *supra* note 50. McHugh suggests that in the area of rate regulation of automobile insurance, open competition subject to the antitrust laws (accomplished through an amendment to the McCarran Act) would provide an alternative to rate regulation by state rating bureaus. *See also* STATE OF NEW YORK INSURANCE DEPARTMENT, THE PUBLIC INTEREST NOW IN PROPERTY AND LIABILITY INSURANCE REGULATION pt. IV, at 132-50 (1969).
52. 359 F. Supp. at 896.
53. 393 U.S. 453 (1969).
54. 15 U.S.C. § 77 (1970).
55. 252 F. Supp. 623 (D. Ariz. 1966).

circuit affirmed on the basis that the action was barred by the McCarran Act.[56] The Supreme Court reversed, holding that the Act did not preclude federal regulation of the relationship between the insurance company and its stockholders because such regultion was not a regulation of the "business of insurance:"[57]

> [W]hatever the exact scope of the statutory term, it is clear where the focus [of the McCarran Act] was—it was on the relationship between the insurance company and the policyholder. Statutes aimed at protecting or regulating this relationship, directly or indirectly, are laws regulating the "business of insurance."[58]

In *American General* the court concluded that the merger did not touch the company-policyholder relationship and therefore was not part of the "business of insurance":

> The relationship involved in the merger of insurance companies is in essence one between individual companies and between those companies seeking to merge and the industry as a whole. State

56. 387 F.2d 25 (9th Cir. 1967).
57. 393 U.S. at 460. The Court went on to discuss the fact that the state of Arizona had approved the merger which the FTC sought to unwind. The Court viewed the approved merger as a secondary issue since the primary focus of the complaint was the misrepresentations made to the stockholders. It had been contended that any attempt to interfere with a merger approved by state insurance officials would be a violation of the McCarran Act. The Court, however, found it could not accept "this overly broad restriction on federal power." *Id.* at 463. For recent discussions of state regulation of mergers, see Fry v. John Hancock Mut. Life Ins. Co., 355 F. Supp. 1151 (N.D. Tex. 1973) (relying on *National Securities*, the court stated that "any state statutes purporting to regulate antitrust aspects of insurance company lending . . . would be antitrust regulation rather than insurance regulation." *Id.* at 1153) and Commander Leasing Co. v. Transamerica Title Ins. Co., 477 F.2d 77 (10th Cir. 1973) (interpreting *National Securities* as saying mergers are not a "part and parcel of the 'business of insurance.'" *Id.* at 85).
58. 393 U.S. at 460. This emphasis on the relationship between the insurance company and the policyholder is uniform throughout those cases interpreting the term "business of insurance." *See* Fry v. John Hancock Mut. Life Ins. Co., 355 F. Supp. 1155 (N.D. Tex. 1973) (a tie-in arrangement whereby those requesting farm loans were required to purchase irrigation systems and/or life insurance policies as a condition of obtaining the loan was not part of the "business of insurance"); De Voto v. Pacific Fidelity Life Ins. Co., 354 F. Supp. 874 (N.D. Cal. 1973) (competing for a list of customers was not part of the "business of insurance"); Hill v. Nat'l Auto Glass Co., 293 F. Supp. 295 (N.D. Cal. 1968) (securing for particular glass dealers the business of an insurance company was not part of the "business of insurance"). *Cf.* Nankin Hosp. v. Michigan Hosp. Serv., 361 F. Supp. 1199 (E.D. Mich. 1973) (providing prepaid hospital care is part of the "business of insurance"); Travelers Ins. Co. v. Blue Cross, 481 F.2d 80 (3d Cir. 1973) (Blue Cross' relationship with hospitals is part of the "insurance business").

> anti-trust statutes seek to deal with the competitive aspects of these mergers, certainly a subject far removed from the relationship between the insurance company and the policyholder contemplated in *National Securities* as constituting the "business of insurance" . . . .[59]

In characterizing the relationship in this manner, the court may have forced the conclusion without adequately evaluating the relationships involved. *National Securities* is authority only for the proposition that the "business of insurance" is concerned primarily with the relationship between the insurance company and the policyholder. Under the facts of that case, the relationship involved was clearly one between the insurance company its stockholders. On the other hand, the relationship to be protected by the regulation of merger activity can be characterized in at least two ways.

First, the relationship could be characterized as one between the merging companies and between the industry and the merging companies as the court did in *American General.* This would be the result if the emphasis is placed on guarding against the evils of "bigness" and protecting the free entry of smaller companies into the market place. Second, the relationship might be characterized as one between the insurance company and the policyholder—a result the court rejected in *American General.* One of the purposes of regulating mergers is the protection of the consumer, which in the case of the insurance industry includes the policyholder. It is the policyholder who in the final analysis would be the victim of a lessening of competition. This characterization assumes that the insurance industry is competitive in the first place, for if the business of insurance is operated as a regulated industry, the consumer-policyholder may be adequately protected regardless of the anti-competitive effects of mergers. This illustrates once more the possibility of inconsistencies when Clayton Act concepts are applied to the business of insurance.[60]

In summary, the court in *American General* may have been too hasty in concluding that the relationship involved in the merger was not one between the insurance company and the policyholder. By choosing to characterize the relationship as it did, the court in effect predetermined the result without considering other possible concerns of the Clayton Act.

CONCLUSION

Merger activity has become increasingly prevalent in the insurance industry. In the face of continuing acquisitions through

59. 359 F. Supp. at 896-97.
60. *See* notes 45-47 and accompanying text *supra*.

mergers and holding company schemes, the question of state versus federal regulation becomes very important. By applying traditional McCarran Act principles to the regulation of insurance company mergers, the court in *American General* overlooked possible conflicts between the theory and practice of insurance regulation. Further elaboration will be necessary before the conflict between federal and state regulation of merger activity is finally resolved.

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