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Regulation of the Insurance Industry After *Hartford Fire Insurance v. California*: The McCarran-Ferguson Act Antitrust Policies

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Regulation of the Insurance Industry After *Hartford Fire Insurance v. California*: The McCarran-Ferguson Act and Antitrust Policies

*Charles R. McGuire**

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I. INTRODUCTION

Traditionally, regulation of the insurance industry in the United States has been left to the individual states. In an attempt to establish a division between federal and state authority to regulate the insurance industry, Congress passed the McCarran-Ferguson Act of 1945¹ ("the Act"), which granted antitrust immunity to certain activities of insurance companies. Based extensively on state law, the system of insurance regulation established under the McCarran-Ferguson Act cannot continue much longer, for it has created a patchwork system of state regulatory schemes, a loss of competitiveness to firms that compete internationally, and tangled bureaucratic and legal thickets for consumers, regulators, and firms which deal across state lines. More importantly, the current system has also resulted in ineffective insurance regulation and a lack of affordable insurance protection for major segments of our economy. On the other hand, suggestions of federal regulation raise the specter of heavy-handed bureaucracy, lack of flexibility, and a diminution of influence for thousands of small, local insurance companies.

A series of insurance crises in the 1980s provided substantial fodder for action by both consumer and legislative groups.² State legisla-

1. An Act to Express the Intent of Congress with Reference to the Regulation of the Business of Insurance, ch. 20, 59 Stat. 33 (1945) ("McCarran-Ferguson Act") (codified as amended at 15 U.S.C. §§ 1011-1015 (1988)). For the pertinent text of the McCarran-Ferguson Act, see *infra* note 29.

2. The various insurance problems and crises began in the early 1980s and progressed throughout the decade. See, e.g., *Price-Cutting Bleeds the Casualty Insurers*, BUSINESS WEEK, Nov. 8, 1982, at 88-95; Resa W. King, *The Coverage Crisis at Town Hall*, BUSINESS WEEK, Aug. 26, 1985, at 72-75; *The Insurance Crisis: Now Everyone is in a Risky Business*, BUSINESS WEEK, March 10, 1986, at 88-92; Christopher Farrell et al.,

tures, in particular, jumped into the fray, providing what many believe to be unfair and burdensome laws in some states and laws that unduly favor insurance companies in other states.³ Moreover, strong elements in Congress, reacting in part to the inability of the current system to adequately regulate the insurance industry, have indicated a desire to amend or even repeal the McCarran-Ferguson Act, thereby subjecting the insurance industry to additional federal legislation, particularly the antitrust laws under the Sherman Act.⁴ As demonstrated by these recent legislative efforts to amend or even repeal the McCarran-Ferguson Act, the existing jerrybuilt scheme of insurance regulation constructed under the McCarran-Ferguson Act has satisfied no one.

In 1993, the United States Supreme Court issued its long-awaited opinion in *Hartford Fire Insurance Co. v. California*.⁵ This case presented an opportunity for an expansion of congressional regulatory power over the insurance industry through a broader interpretation of the McCarran-Ferguson Act and provided some hope for a more coherent and effective system of insurance regulation. The Court's jumbled opinion, however, failed to seize that opportunity. Instead, the *Hartford Fire Insurance* case illustrated the impracticability of state regulation of the insurance industry, and the Court's opinion emasculated the already limited ability of the federal government to regulate the insurance industry. Thus, the *Hartford Fire Insurance* opinion did nothing to alter the confused and patchwork scheme of insurance regulation established by the McCarran-Ferguson Act.

In the wake of the *Hartford Fire Insurance* decision, it is time for a

The Crisis is Over—But Insurance Will Never Be the Same, BUSINESS WEEK, May 25, 1987, at 122-23; Ronald Grover et al., *They're Watching This California Brawl from Coast to Coast*, BUSINESS WEEK, Feb. 15, 1988, at 34.

In the early 1990s the problem of insolvency came to the forefront. See, e.g., Jeffrey A. Koepfel, *The Insolvency Looking Glass*, BEST'S REVIEW, Sept. 1991, at 23-30; Evelyn Gilbert, *Company Insolvencies Wreak Havoc*, NATIONAL UNDERWRITER, Nov. 18, 1991, at 29.

3. Probably the best-known example of such a state law is Proposition 103, passed in California in November 1988. Proposition 103 was a referendum that cut all automobile insurance rates in the state by 20%. Major regulatory overhauls, based in part on Proposition 103, were considered or are underway in Georgia, Maryland, Michigan, New Jersey, Pennsylvania, Texas, and Washington. See Eric Schine, *It's Second and Ten for Prop 103*, BUSINESS WEEK, Feb. 11, 1991, at 68. Other states responded to the problems differently by adopting various types of tort "reform" to restrict recoveries by injured parties.

4. 15 U.S.C. §§ 1-7 (1988).

5. 113 S. Ct. 2891 (1993). The case has progressed through a series of names. Before the Ninth Circuit Court of Appeals and the district court, it was called *In re Insurance Antitrust Litig.*, 938 F.2d 919 (9th Cir. 1991), *rev'g* 723 F. Supp. 464 (N.D. Cal. 1989).

fresh look at the McCarran-Ferguson system of insurance regulation. The world economy has become increasingly interdependent over the past fifty years, and the financial community—including the insurance industry—has led the way. The reinsurance and retrocessional insurance markets are now clearly global, as are markets for excess surplus lines and other exceptional risks. Moreover, major American firms are increasingly expanding their operations into foreign countries. Today, the insurance industry is not a single industry, but rather a polyglot group of separate industries and divisions of other financial institutions that are not closely related to one another except by the common and generic name “insurance.” Regulation of these varied industries is essential, and in many cases regulation should be consistent across the nation, a requirement that generally calls for federal oversight. On the other hand, regulation must also be flexible enough to accommodate the heterogeneous demands of the various businesses we call “insurance,” for important aspects of the insurance industry demand more local control and regulation than can be obtained through federal action.⁶

The purpose of this article is to begin a dialogue toward that fresh look. Part II reviews the history and background of insurance regulation in the United States, including the theories behind the grant of a limited antitrust exemption to the insurance industry, the passage and subsequent interpretations of the McCarran-Ferguson Act, and judicially created doctrines that limit federal authority to regulate the insurance industry. Part II also considers the application of the “state action” rule, which allows states to displace federal antitrust regulation through state law, and the doctrine of international comity. Part III traces the *Hartford Fire Insurance* case, including its jumbled procedural history and complex holding, both of which derive, at least in part, from the crazy-quilt compromise nature of the McCarran-Ferguson Act. Part IV analyzes the effect of the Supreme Court’s *Hartford Fire Insurance* decision on the McCarran-Ferguson Act system of insurance regulation, summarizes the problems of insurance regulation in the current hybrid environment, and urges that the current system of insurance regulation be revised to reject complete control by either the states or the federal government. This Article concludes by taking the position that the system of insurance regulation should embrace a creative use of uniform laws, interstate compacts, and federally-mandated state regulation in a flexible and realistic manner.

6. For example, regulation and licensing of insurers and brokers are almost certainly best accomplished by state authorities. Similarly, regulation of the thousands of small, local mutual insurance companies is far more efficiently done at the state level.

II. HISTORY AND BACKGROUND OF INSURANCE REGULATION IN THE UNITED STATES AND THE MCCARRAN-FERGUSON ACT

The authority to regulate the insurance industry in the United States has traditionally been within the province of the states rather than the federal government. An early interpretation of the Commerce Clause⁷ essentially barred the federal government from exercising authority over the insurance industry and left this regulatory power to the states.⁸ As the definition of "interstate commerce" and interpretations of congressional power to regulate commerce pursuant to the Commerce Clause evolved, it came to appear that the federal government would in fact be able to regulate the insurance industry.⁹ Congress responded by passing the McCarran-Ferguson Act,¹⁰ which not only recognized the authority of the states to regulate the insurance industry but also granted a limited exemption from federal antitrust laws to the "business of insurance."¹¹ As a result of this regulatory void and the McCarran-Ferguson Act's invitation to states to regulate the insurance industry, states have enacted a wide variety of schemes to tax and regulate the insurance business.

A. Congressional Power to Regulate the Insurance Industry

Any history of regulation of the insurance industry in the United States must begin with *Paul v. Virginia*.¹² In *Paul*, the United States Supreme Court held that "[i]ssuing a policy of insurance is not a transaction of commerce," and that the business of insurance was therefore beyond the scope of the Commerce Clause.¹³ A number of subsequent

7. U.S. CONST. art. I, § 8, cl. 3.

8. See *Paul v. Virginia*, 75 U.S. (8 Wall.) 168, 183-85 (1868) (holding that insurance contracts "are not articles of commerce in any proper meaning of the word" and are instead "local transactions . . . governed by the local law"); see also *infra* part II.A.

9. See *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533, 541, 553 (1944) (recognizing that the business of insurance results in "a continuous and indivisible stream of intercourse among the states" and reasoning that "[n]o commercial enterprise of any kind which conducts its activities across state lines has been held to be wholly beyond the regulatory power of Congress under the Commerce Clause"); see also *infra* part II.A.

10. Ch. 20, 59 Stat. 33 (1945) (codified as amended at 15 U.S.C. §§ 1011-1015 (1988)).

11. See §§ 2-3, 59 Stat. at 34.

12. 75 U.S. (8 Wall.) 168 (1868).

13. *Id.* at 183. Explaining its refusal to characterize "contracts of insurance" as commerce, the *Paul* Court stated:

These contracts are not articles of commerce in any proper meaning of the word. They are not subjects of trade and barter offered in the market as something having an existence and value independent of the parties to them. They are not commodities to be shipped or forwarded from one State to another, and

cases reinforced the notion that insurance was outside federal regulatory power because it was not “commerce” within the meaning of the Commerce Clause.¹⁴

The Supreme Court’s initial interpretation of the Commerce Clause precluded the federal government from regulating the insurance industry for nearly eighty years until 1944 when the Court decided the seminal case of *United States v. South-Eastern Underwriters Ass’n*.¹⁵ In *South-Eastern Underwriters*, antitrust indictments were brought against the South-Eastern Underwriters Association, its membership of nearly two hundred private stock fire insurance companies, and twenty-seven individuals for alleged violations of the Sherman Act.¹⁶ The defendants challenged the indictments on the basis of *Paul v. Virginia* and its progeny, arguing that in light of the Court’s prior holding that insurance contracts do not involve interstate commerce, regulation of the insurance industry was beyond congressional power.¹⁷ The *South-Eastern Underwriters* Court departed from its prior characterization of “contracts of insurance,” however, and held that the business of insurance was indeed “commerce” within the meaning of the Commerce Clause and that it therefore could be regulated by the federal government.¹⁸ After reviewing the legislative

then put up for sale. They are like other personal contracts between parties which are completed by their signature and the transfer of the consideration. Such contracts are not inter-state transactions, though the parties may be domiciled in different States. The policies do not take effect—are not executed contracts—until delivered by the agent in Virginia. They are, then, local transactions, and are governed by the local law. They do not constitute a part of the commerce between the States any more than a contract for the purchase and sale of goods in Virginia by a citizen of New York whilst in Virginia would constitute a portion of such commerce.

Id. Thus, the Court effectively placed the insurance industry beyond the reach of federal regulation and the Commerce Clause.

14. *See, e.g.*, *New York Life Ins. Co. v. Deer Lodge County*, 231 U.S. 495, 510 (1913) (holding that the business of insurance involves neither state nor interstate commerce); *Hooper v. California*, 155 U.S. 648, 655 (1895) (holding that “[t]he business of insurance is not commerce”). These cases reflect the Court’s restrictive interpretation of the Commerce Clause in the late 19th and early 20th centuries. Given the decisions by the courts in 1937 following Franklin Roosevelt’s failed attempt to “pack” the Supreme Court, a more expansive reading of the Commerce Clause was virtually inevitable. *See Helvering v. Davis*, 301 U.S. 619 (1937); *NLRB v. Jones & Laughlin Steel Corp.*, 301 U.S. 1 (1937); *West Coast Hotel Co. v. Parrish*, 300 U.S. 379 (1937).

15. 322 U.S. 533 (1944).

16. *Id.* at 534. The parties were indicted for two alleged violations of the Sherman Act: (1) a conspiracy to restrain interstate trade and commerce by fixing premiums on certain lines of insurance; and (2) a conspiracy to monopolize trade and commerce in those same lines of insurance. *Id.* at 534-35.

17. *Id.* at 536, 543-45.

18. *South-Eastern Underwriters*, 322 U.S. at 553. The Court noted that in every case

history of the Sherman Act, the Court concluded that Congress did not intend to exempt insurance companies from the application of the Sherman Act.¹⁹ Thus, following *South-Eastern Underwriters*, it appeared that the federal government did indeed have the power to regulate the insurance industry through the antitrust laws. Moreover, and perhaps most disturbing to the insurance industry, *South-Eastern Underwriters* made it clear that Congress could pass legislation specifically for the purpose of regulating the insurance industry.

B. Theories of Exemption for the Insurance Industry

Although robust competition is the theoretical norm for both capitalism and the antitrust laws,²⁰ completely unrestricted competition can sometimes result in specific abuses and structural problems that may in fact threaten capitalism. As a result, a variety of regulatory schemes have been developed in various industries to eliminate or soften any specific abuses or structural problems.

Commentators have recognized that the unique nature of the insurance industry presents special regulatory problems, particularly with regard to the effect of competition within the industry. For instance, it has often been argued that vigorous competition in the insurance industry would lead to inadequate premium rates and the insolvency of many insurance companies.²¹ Rate competition would allegedly lead to inadequate rate levels, rate discrimination, and insolvency, thereby

in which it had held that "the business of insurance is not commerce," it had been faced with the issue of the validity of a state statute regulating the insurance industry. *Id.* at 544. In fact, the Court had never before addressed the validity of an attempt by Congress to regulate the insurance industry. *Id.* Accordingly, the Court noted that its prior characterizations of insurance as outside the scope of "commerce" had occurred in cases where the Court was evaluating state rather than federal regulations, and observed that such characterizations were "inconsistent with many decisions of [the] Court which have upheld federal statutes regulating interstate commerce under the Commerce Clause." *Id.* at 545 (footnote omitted).

19. *South-Eastern Underwriters*, 322 U.S. at 560-61.

20. One must remember that the purpose of the antitrust laws is to foster capitalism, not restrict it:

The American antitrust laws are essentially conservative in nature. Their purpose is to maintain free competition by insuring that such competition is fair. They seek to prevent giant aggregations of economic power from being built unfairly, because the use of such power necessarily stifles the opportunities competitors will have to compete meaningfully. In summary, the antitrust laws seek to prevent conduct which weakens or destroys competition.

EARL W. KINTNER, AN ANTITRUST PRIMER 15 (2d ed. 1973).

21. Earl W. Kintner et al., *Application of the Antitrust Laws to the Activities of Insurance Companies: Heavier Risks, Expanded Coverage, and Greater Liability*, 63 N.C. L. REV. 431, 432 (1985).

resulting in "financial chaos and public injury."²² As one authority on antitrust has observed:

A substantial part of the problem is that an insurer may have difficulty assessing the risks involved and hence the magnitude of claims that it may have to pay. Thus, although premiums define the insurer's income, its costs or expenses are far less predictable. If an insurer underestimates the claims it will have to pay, it may not have sufficient funds to pay them. This uncertainty will lead either to a lack of adequate coverage, insolvency of the company, or both.²³

To address these problems, insurance companies often base their rates on actuarial and statistical projections of loss. Rating organizations in the property and casualty insurance industry obtain loss data from member firms and provide loss projections to their member companies. Arguably, such statistical sharing provides more stability for insurance companies and more precise rates for consumers.²⁴

The principle rating bureau for the property and liability insurance field is the Insurance Services Office (ISO), a national rating bureau that computes rates for most lines of property and liability insurance.²⁵ Although no such organization exists in the life insurance industry, the Society of Actuaries likewise exchanges information among its members, thus performing much the same function.²⁶ Nevertheless,

22. *South-Eastern Underwriters*, 322 U.S. at 561; see also JOHN G. DAY, *ECONOMIC REGULATION OF INSURANCE IN THE UNITED STATES* 18 (1970) (noting that "[r]ate setting in concert" has historically been the insurance industry's answer to the perceived dangers of inadequate rate levels, rate discrimination, and insolvency).

Nevertheless, one commentator argues that the insurance industry is in fact quite competitive for two reasons: (1) that there is a significant portion of the market that is controlled by nonbureau companies that develop their own rates and price their products individually; and (2) bureau pricing simply moves competition from price to underwriting. That is, while the price charged to consumers may be fixed, insurer's costs may vary from those on which the bureau's rates are predicted, so insurers alter their underwriting standards by insuring or rejecting riskier activities at the same cost. See EMMETT J. VAUGHN, *FUNDAMENTALS OF RISK AND INSURANCE* 97 (6th ed. 1992).

23. Kintner et al., *supra* note 21, at 433 n.10.

24. VAUGHN, *supra* note 22, at 75.

25. *Id.* at 94. In May of 1989, however, ISO announced its decision to stop providing advisory rates to its members and to provide only trended loss costs. Consequently, companies will be required to develop their own factors for expenses, profits and contingencies. *Id.* at 97. This change was adopted, at least in part, due to criticisms that the activities of rating bureaus consisted of price-fixing behavior and that such cooperation among insurance companies indicated the possible existence of a cartel. *Id.*

26. The Society of Actuaries is a professional organization of life and health insurance actuaries. The organization, like many professional groups, has a number of meetings and proceedings and produces research papers and publications that provide for an exchange of actuarial information and for the establishment of standards for their profession.

the uncertainty in assessing risk and potential claims is undoubtedly more serious for property and liability insurers than for health or life insurers, for the latter insurers have the advantage of actuarial tables, health statistics, and other predictors that make their risk assessment far easier.²⁷

*C. Congressional Regulation of the Insurance Industry:
The McCarran-Ferguson Act*

In 1945, following the Court's ruling in *South-Eastern Underwriters* and as a result of lobbying by the National Association of Insurance Commissioners ("NAIC"),²⁸ Congress passed the McCarran-Ferguson Act.²⁹ The concerns that prompted the enactment

27. Kintner et al., *supra* note 21, at 433 n.10. Consequently, it may be argued that health and life insurers may be less deserving of antitrust immunity. *Id.*

28. See Julia M. Melendez, *The McCarran-Ferguson Act: Has It Outlived Its Intent?* 42 FED'N INS. & CORP. COUNS. Q. 283, 286-87 (1992); see also Charles D. Weller, *The McCarran-Ferguson Act's Antitrust Exemption for Insurance: Language, History and Policy*, 1978 DUKE L. J. 587, 592 (noting that Congress considered legislation regarding federal regulation of the insurance industry even prior to the Court's decision in *South-Eastern Underwriters*). For an exhaustive analysis of the legislative history of the McCarran-Ferguson Act, see Weller, *supra*.

29. Ch. 20, 59 Stat. 33 (1945) (codified as amended at 15 U.S.C. §§ 1011-1015 (1988)). The current version of the Act provides in pertinent part:

§1011. Declaration of policy

Congress hereby 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.

§1012. Regulation by State law; Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948

(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 . . . 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.

15 U.S.C. §§ 1011-1012 (1988).

Section 3(b) of the Act provides in pertinent part:

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.

15 U.S.C. § 1013(b).

of the McCarran-Ferguson Act appear to have been threefold: first, that the application of the antitrust laws to the insurance industry was wholly inappropriate and that an exemption from those laws was required to protect insurers from criminal antitrust liability; second, that state schemes taxing and regulating insurance would be found to violate the Commerce Clause as the Court had interpreted it in *South-Eastern Underwriters*; and third, that legislation was needed to erect a barrier against the perceived threat that the "activist Roosevelt administration" would federalize insurance regulation and wrest control from the states.³⁰

In view of these concerns, Congress provided in the McCarran-Ferguson Act that federal antitrust laws would apply to the business of insurance, but only in specific circumstances.³¹ Under McCarran-Ferguson, Congress gave the insurance industry a *conditional* exemption from federal antitrust laws. The McCarran-Ferguson Act exempts only (1) the business of insurance; (2) *to the extent* that such business is regulated by state law; and (3) so long as no boycott, intimidation, or coercion takes place.³² The limited nature of this exemption is illustrated by the legislative history of a bill that Congress considered and rejected before it adopted McCarran-Ferguson.

Immediately prior to the enactment of the McCarran-Ferguson Act, Congress had considered the Walter-Hancock bill,³³ which would have completely exempted the insurance industry from federal antitrust laws. The Walter-Hancock bill passed the House and initially passed

As adopted, the Act is deceptively simple in form; however, it touches issues affecting the entire insurance industry and the regulatory schemes of all of the states as well as that of the federal government.

30. Weller, *supra* note 28, at 590-91.

31. Soon after enactment of the McCarran-Ferguson Act, the Supreme Court described the Act's purpose:

Obviously Congress' purpose was broadly to give support to the existing and future state systems for regulating and taxing the business of insurance. This was done in two ways. One was by removing obstructions which might be thought to flow from its own power, whether dormant or exercised, except as otherwise expressly provided in the Act itself or in future legislation. The other was by declaring expressly and affirmatively that continued state regulation and taxation of this business is in the public interest and that the business and all who engage in it "shall be subject to" the laws of the several states in these respects.

Prudential Ins. Co. v. Benjamin, 328 U.S. 408, 429-30 (1946).

32. 15 U.S.C. §§ 1011-1013. See *St. Paul Fire & Marine Ins. Co. v. Barry*, 438 U.S. 531, 539 (1978), discussed *infra* notes 54-70 and accompanying text; *SEC v. National Sec., Inc.*, 393 U.S. 453, 458-60 (1969), discussed *infra* notes 49-53 and accompanying text; *FTC v. National Casualty Co.*, 357 U.S. 560, 563 (1958), discussed *infra* notes 47-48 and accompanying text.

33. H.R. 3270, 78th Cong., 1st Sess. (1943).

the Senate, but the Senate later reconsidered and rejected the bill.³⁴ Shortly thereafter, Congress adopted the McCarran-Ferguson Act, which was the replacement bill for Walter-Hancock. Significantly, McCarran-Ferguson contained a provision that the rejected Walter-Hancock bill had not: that the federal antitrust laws would indeed apply to the business of insurance in specific instances.³⁵ This limited exemption from the antitrust laws is a far cry from the absolute exemption that the Walter-Hancock bill had embraced. Therefore, the adoption of the McCarran-Ferguson Act, which Congress passed in lieu of the Walter-Hancock bill, reflects Congress's view that the states' authority to regulate the business of insurance is not exclusive.³⁶ The conditional and ambiguous nature of the insurance industry's limited exemption has become the basis for much litigation, including the *Hartford Fire Insurance* case, and is the focus of this Article.

D. Eroding State Power: Judicial Treatment of the McCarran-Ferguson Act Prior to Hartford Fire Insurance

Over the years, judicial examination of the McCarran-Ferguson Act has focused on three major issues: (1) the nature of the Act's "business of insurance" exemption;³⁷ (2) the division of regulatory

34. See 90 Cong. Rec. 6565, 8054 (1943).

35. See §§ 2-3, 59 Stat. at 34. The provision of a conditional exemption was partially a result of lobbying efforts by the NAIC, which sought both continued state regulation of the insurance industry and the application of the antitrust laws to conduct not necessary for the welfare of policy owners. Melendez, *supra* note 28, at 286. Stock insurance companies opposed any application of federal antitrust laws to the business of insurance and preferred the Walter-Hancock bill. *Id.* These opposing views demonstrate that the insurance industry is neither monolithic nor unanimous. There are dozens of types of insurance, including health, life, auto, property, worker's compensation, casualty, liability and others, and sub-groups within each type. Stock companies differ widely from mutual companies. Various insurance professionals, including brokers and producers, primary insurers, reinsurers, and retrocessional insurers, often have differing interests. Companies range in size from small "Mom and Pop" local mutuals to giants of the industry. Additionally, there are an incredible number of professional organizations, continuing education programs, industry groups, lobbying organizations and other groups. To assume that any common interest exists within this group is extremely risky, and probably inaccurate.

36. See Melendez, *supra* note 28, at 287. It is also possible that the historical purpose of the McCarran-Ferguson Act was simply to codify the existing state action doctrine under *Parker v. Brown*, 317 U.S. 341 (1943). See Weller, *supra* note 28, at 615-19. See *infra* part II.F.1 for a discussion of *Parker v. Brown* and the state action doctrine.

37. See *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982), discussed *infra* notes 85-86 and accompanying text; *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205 (1979), discussed *infra* notes 71-84 and accompanying text.

authority between the states and the federal government;³⁸ and (3) the definition of the terms "boycott, coercion, or intimidation."³⁹ Although the Court's recent decision in *Hartford Fire Insurance* focused primarily on the third of these issues, the Court has previously considered the first two issues at length.

In the course of its examination of the McCarran-Ferguson Act, the Supreme Court has sought to balance the degree to which federal and state governments may regulate the business of insurance. Although the Court's decisions have often centered on rather specific issues of statutory interpretation, the historical trend of the Court has been to move away from state regulation and to recognize greater federal regulatory power over the insurance industry. The high water mark of federal regulation may have come and gone, however, for in *Hartford Fire Insurance* the Court placed some limits on federal authority.⁴⁰

The Court first examined the McCarran-Ferguson Act in *Prudential Insurance Co. v. Benjamin*,⁴¹ in which it considered the division between state and federal authority to regulate the insurance industry as it upheld a South Carolina tax on out-of-state insurers.⁴² In *Benjamin*, Prudential Insurance Co., a New Jersey corporation, challenged a South Carolina law that taxed premiums received by foreign insurance companies from business done in South Carolina.⁴³ Prudential contended that because the statute did not place a similar tax on premiums paid to domestic insurers, it violated the Commerce Clause by discriminating against interstate commerce.⁴⁴ The Court rejected Prudential's argument and noted that the McCarran-Ferguson Act did not require uniformity of regulation and taxation with respect to the insurance industry.⁴⁵

Following *Benjamin*, the Supreme Court had no occasion to interpret the Act for about a decade. Later cases affirmed state authority to

38. See *SEC v. National Sec., Inc.*, 393 U.S. 453 (1969), discussed *infra* notes 49-53 and accompanying text; *FTC v. National Casualty Co.*, 357 U.S. 560 (1958), discussed *infra* notes 47-48 and accompanying text; *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408 (1946), discussed *infra* notes 41-45 and accompanying text.

39. See *St. Paul Fire & Marine Ins. Co. v. Barry*, 438 U.S. 531 (1978), discussed *infra* notes 54-70 and accompanying text.

40. For a thorough discussion of the way in which the *Hartford Fire Insurance* decision limits federal authority to regulate the insurance industry, see *infra* part III.

41. 328 U.S. 408 (1946).

42. See *id.* at 427-40.

43. *Id.* at 410.

44. *Id.* at 411.

45. See *Benjamin*, 328 U.S. at 431, 433-36. The *Benjamin* Court also recognized that Congress's power over interstate commerce includes, with some limitation, the power to discriminate against interstate commerce and in favor of local trade. *Id.* at 434.

regulate and tax the insurance industry and, to some degree, countered fears that states would be stripped of the power to regulate and tax.⁴⁶ For example, in *FTC v. National Casualty Co.*,⁴⁷ the Court held that the Federal Trade Commission did not have authority to regulate advertising of insurance at a local level because such matters had effectively been left to the states.⁴⁸

Beginning in 1969, the Court began to recognize greater federal regulatory power over the insurance industry. In *SEC v. National Securities, Inc.*,⁴⁹ the Court addressed the argument that the McCarran-Ferguson Act prohibited the SEC from bringing an action for fraud under the federal Securities Exchange Act against the controlling shareholder of an insurance company.⁵⁰ The controlling shareholder argued that because the state director of insurance found, pursuant to a state statute, that a proposed merger would not be inequitable to the shareholders of the insurance companies involved in the merger, the SEC could not supersede state law by suing under the federal Securities Exchange Act.⁵¹ The Court distinguished between “insurance” regulation and “securities” regulation and found the latter not to be within the scope of the McCarran-Ferguson Act.⁵² Because the Court found that the state statute constituted an attempt to protect purchasers of securities rather than purchasers of insurance policies, it held that the McCarran-Ferguson Act did not bar the SEC from bringing the action.⁵³

The Court again recognized federal regulatory power over the insur-

46. See Francis Achampong, *The McCarran-Ferguson Act and the Limited Insurance Antitrust Exemption: An Indefensible Aberration?* 15 SETON HALL LEGIS. J. 141, 150 (1991).

47. 357 U.S. 560 (1958).

48. *Id.* at 564; see also *Wilburn Boat Co. v. Fireman's Fund Ins. Co.*, 348 U.S. 310 (1955) (rejecting an insurer's contention that federal admiralty law controlled a case involving a claim on a marine insurance contract and holding instead that Texas law governed); Weller, *supra* note 28, at 599-600. But see *SEC v. Variable Annuity Life Ins. Co.*, 359 U.S. 65 (1959). In *Variable Annuity Life Ins. Co.*, the Court ruled by a five-to-four margin that variable annuities were not “insurance” within the meaning of the McCarran-Ferguson Act and therefore could be regulated by the federal authorities. See *id.* at 71-73. The narrow margin and rather convoluted means by which the Court held that the Securities and Exchange Commission had authority to regulate the variable annuities indicates the reverence with which state authority over insurance was viewed in the 1950s.

49. 393 U.S. 453 (1969).

50. *Id.* at 455-57.

51. *Id.* at 457.

52. *Id.* at 460.

53. *Id.*

ance industry in *St. Paul Fire & Marine Insurance Co. v. Barry*,⁵⁴ the case in which the Supreme Court first defined the term “boycott” within the context of the McCarran-Ferguson Act. In *Barry*, a group of Rhode Island physicians and patients brought an antitrust action against four insurance companies that sold medical malpractice insurance.⁵⁵ The complaint alleged that three of the four insurance companies—the only providers of medical malpractice insurance in the state—had refused to accept applications for insurance from the policyholders of the fourth insurer in an attempt to compel them to submit to new policy provisions established by the fourth insurer.⁵⁶ In effect, policyholders of the fourth insurer who would not submit to the changes were thereby precluded from obtaining coverage from any insurer in Rhode Island.⁵⁷

The *Barry* plaintiffs alleged that this scheme amounted to a boycott that was not immunized from federal antitrust scrutiny by the McCarran-Ferguson Act.⁵⁸ The defendants, however, argued that the term “boycott,” as used in the McCarran-Ferguson Act, “should be limited to cases where concerted refusals to deal are used to exclude or penalize insurance companies or other traders which refuse to conform their competitive practices to terms dictated by the conspiracy.”⁵⁹ After the court of appeals reversed the district court’s decision to dismiss the complaint,⁶⁰ the Supreme Court granted certiorari to consider the meaning of the term “boycott” in the context of the McCarran-Ferguson Act.⁶¹

The Supreme Court began its analysis by tracing the language and

54. 438 U.S. 531 (1978).

55. *Id.* at 533.

56. *Id.* The major changes sought by the fourth insurer included the elimination of coverage on an “occurrence” basis and the limiting of coverage on a “claims-made” basis. *Id.* at 535. Note the similarity to the motivation and the desired policy changes in the *Hartford Fire Insurance* case.

57. *Id.* at 553.

58. *Barry*, 438 U.S. at 533-36.

59. *Id.* at 540 (quoting Brief for Petitioners at 13, *Barry* (No. 77-240)).

60. *Barry v. St. Paul Fire & Marine Ins. Co.*, 555 F.2d 3, 8 (1st Cir. 1977). In granting the defendant’s motion to dismiss, the district court concluded that the conduct did not amount to a boycott under the McCarran-Ferguson Act, stating instead that “the purpose of the boycott, coercion, and intimidation exception was solely to protect insurance agents or other insurance companies from being ‘black-listed’ by powerful combinations of insurance companies, not to affect the insurer-insured relationship.” *See Barry*, 438 U.S. at 536 (quoting the district court’s unpublished opinion). The court of appeals reversed, assigning the term “boycott” its “normal Sherman Act scope” by defining the term as any “concerted refusal to deal” with a disfavored purchaser or seller. *Barry*, 555 F.2d at 7.

61. *See Barry*, 438 U.S. at 534.

history of the McCarran-Ferguson Act.⁶² The Court then reasoned that the term “boycott” should be interpreted in light of its traditional meaning, as elaborated by decisions interpreting the Sherman Act.⁶³ Based upon its analysis of those decisions, the Court concluded that under the traditional antitrust meaning of the term, the defendant’s activities indeed constituted a “boycott.”⁶⁴

The *Barry* Court also considered whether the legislative history of the Act indicated that Congress intended to attach a special meaning to the word “boycott” apart from its established Sherman Act meaning.⁶⁵ After discussing a number of specific legislative comments by key representatives, the Court emphasized that section 3(b) of the Act contained broad and unqualified language.⁶⁶ The Court reasoned that had Congress intended to preclude policyholders from bringing Sherman Act claims by limiting the term “boycott” to the activities of competing insurance companies, it would have explicitly stated this

62. *Id.* at 541.

63. *Id.* The Court examined numerous cases defining boycott in the context of federal antitrust actions, including *Federal Maritime Comm’n v. Aktiebolaget Svenska Amerika Linien*, 390 U.S. 238 (1968); *United States v. General Motors Corp.*, 384 U.S. 127 (1966); *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594 (1953); *Klor’s, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959); *Bedford Cut Stone Co. v. Journeymen Stone Cutters’ Ass’n*, 274 U.S. 37 (1927); *Duplex Printing Press Co. v. Deering*, 254 U.S. 443 (1921); *Gompers v. Buck’s Stove & Range Co.* 221 U.S. 418 (1911); and *Loewe v. Lawler*, 208 U.S. 274 (1908). See *Barry*, 438 U.S. at 541-46.

64. *Barry*, 438 U.S. at 545. In reaching this conclusion, Justice Powell authored a passage for the majority that became the source of debate between the district court and the court of appeals in the *Hartford Fire Insurance* case:

Whatever other characterizations are possible, petitioners’ conduct fairly may be viewed as “an organized boycott[]” of St. Paul’s policyholders. Solely for the purpose of forcing physicians and hospitals to accede to a substantial curtailment of the coverage previously available, St. Paul induced its competitors to refuse to deal on any terms with its customers. This agreement did not simply fix rates or terms of coverage; it effectively barred St. Paul’s policyholders from all access to alternative sources of coverage and even from negotiating for more favorable terms elsewhere in the market. The pact served as a tactical weapon invoked by St. Paul in support of a dispute with its policyholders. The enlistment of third parties in an agreement not to trade, as a means of compelling capitulation by the boycotted group, long has been viewed as conduct supporting a finding of unlawful boycott.

Id. at 544-45 (citations omitted). Despite this broad statement, the Court rejected the idea that the McCarran-Ferguson Act’s use of the term “boycott” was coextensive with that of the Sherman Act. See *id.* at 545 n.18.

65. *Barry*, 438 U.S. at 545-50. The Court noted that the congressional debates “make clear that the ‘boycott’ exception was viewed by the Act’s proponents as an important safeguard against the danger that insurance companies might take advantage of purely permissive state legislation to establish monopolies and enter into restrictive agreements falling outside the realm of state-supervised cooperative action.” *Id.* at 547.

66. *Id.* at 550.

intention.⁶⁷ Accordingly, the Court concluded that the Act covers *any* act constituting a boycott, coercion, or intimidation⁶⁸ and that the term “is not limited to concerted activity against insurance companies or agents or, more generally, against competitors of members of the boycotting group.”⁶⁹ In light of this broad definition of the term “boycott,” the Court held that the actions of the defendant insurers in *Barry* constituted a boycott within the meaning of the McCarran-Ferguson Act.⁷⁰

The trend toward recognizing greater federal regulatory power over the insurance industry continued in *Group Life & Health Insurance Co. v. Royal Drug Co.*,⁷¹ in which the Court clarified the meaning of the term “business of insurance” within McCarran-Ferguson.⁷² In *Royal Drug*, a group of independent pharmacies alleged that defendant Blue Shield, a Texas insurance company, and three pharmacies had violated section 1 of the Sherman Act by conspiring to fix prices of prescription drugs.⁷³ The alleged conspiracy involved “Pharmacy Agreements,” under which Blue Shield’s reimbursement scheme effectively allowed participating pharmacies to offer prescription drugs to customers at a lower price than the independent pharmacies could.⁷⁴ To determine whether the agreements violated federal antitrust laws, the Court questioned whether the agreements constituted a part of the “business of insurance,” within which Blue Shield would be immunized from federal antitrust laws under the McCarran-Ferguson Act.⁷⁵ Noting the express language of the Act, the Court concluded that the Act specifically exempts the “business of insurance” and not “the business of insurers”:

67. *Id.*

68. *Id.*

69. *Barry*, 438 U.S. at 552.

70. *Id.* at 554.

71. 440 U.S. 205 (1979).

72. *Id.* at 232-33.

73. *Id.* at 207. The independent pharmacies also claimed that the alleged conspiracy caused an unlawful group boycott by Blue Shield policyholders. *Id.*

74. *Royal Drug*, 440 U.S. at 209. Under the agreements, the participating pharmacies would furnish prescription drugs to Blue Shield policyholders at \$2.00, and Blue Shield would then reimburse those pharmacies for their cost of acquiring the drugs. *Id.* Thus, Blue Shield policyholders paid only \$2.00 for prescription drugs at participating pharmacies. *Id.* In contrast, at nonparticipating pharmacies, the policyholders paid the full price for prescription drugs, and Blue Shield would reimburse the policyholders for 75% of the drug price over \$2.00. *Id.* As a result, only those nonparticipating pharmacies that could afford to sell prescription drugs for less than the \$2.00 mark-up could profitably provide drugs to Blue Shield policyholders. *Id.*

75. *Royal Drug*, 440 U.S. at 210.

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.” 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 apply.⁷⁶

The *Royal Drug* Court then analyzed the agreements to determine whether they fell within the McCarran-Ferguson exemption and concluded that for several reasons, the actual agreements did not constitute the “business of insurance.” First, the Court noted that the most basic aspect of an insurance contract is the “spreading and underwriting of a policyholder’s risk”⁷⁷ and concluded that the Pharmacy Agreements, which were merely a mechanism for Blue Shield to purchase goods and services cheaply, did not fall within that definition.⁷⁸ Indeed, the Court concluded that the agreements were “legally indistinguishable from countless other business arrangements that may be made by insurance companies to keep their costs low and thereby also keep low the level of premiums charged to their policyholders.”⁷⁹

The Court also noted that the congressional intent underlying the McCarran-Ferguson Act focused on the relationship between insurer and insured, and any additional “activities of insurance companies [that] relate so closely to their status as reliable insurers that they, too, must be placed in the same class.”⁸⁰ At best, the Court concluded, Blue Shield had shown a cost savings that could be passed on to its policyholders.⁸¹ Moreover, the legislative history clearly demonstrated that such collateral agreements were not intended to qualify as the “business of insurance.” References in congressional debates indicated that in permitting the exemption from federal antitrust laws under McCarran-Ferguson, Congress was primarily concerned with the underwriting of risks and with permitting intra-industry cooperation for statistical and rate-making purposes.⁸² Finally, the Court

76. *Id.* at 211 (quoting *National Securities*, 393 U.S. at 459-60).

77. *Royal Drug*, 440 U.S. at 211.

78. *Id.* at 214.

79. *Id.* at 215.

80. *Id.* at 215-16 (quoting *SEC v. National Sec., Inc.*, 393 U.S. 453, 460 (1969)).

81. *Royal Drug*, 440 U.S. at 216.

82. *Id.* at 220-22. Moreover, at the time of the McCarran-Ferguson debates, health insurers “were not considered to be engaged in the insurance business at all.” *Id.* at 226. In fact, to avoid state regulation, Blue Cross and Blue Shield historically took the position that they were not insurance companies. *Id.* at 229.

stated that both implicit and explicit statutory exemptions from the antitrust laws should be narrowly construed.⁸³ The Court then held that the agreements did not constitute a part of the "business of insurance" and consequently were not within the McCarran-Ferguson exemption from the federal antitrust laws.⁸⁴

More recently, in *Union Labor Life Insurance Co. v. Pireno*,⁸⁵ the Supreme Court enumerated specific criteria for determining what constitutes the "business of insurance":

[F]irst, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry.⁸⁶

Thus, the trend from the late 1960s through 1982 reveals a gradual increase in federal authority and a consequent decrease in state authority to regulate the insurance industry. The Court's early interpretations of the McCarran-Ferguson Act, beginning with *Benjamin* in 1946 and continuing through *FTC v. National Casualty Co.* in 1958, appear to have favored the exercise of state regulatory power. Beginning with *National Securities* in 1969, however, the cases reveal the Court's increasing willingness to favor the use of federal authority.

E. Proposals for Legislative Reform of McCarran-Ferguson

Recently, the McCarran-Ferguson Act has come under increasing scrutiny from legislative, judicial, and academic sources.⁸⁷ Some

83. *Royal Drug*, 440 U.S. at 231. According to the Court, a narrow construction of the antitrust exemption provided under McCarran-Ferguson would be particularly appropriate in cases involving agreements outside the insurance industry. *Id.* The Court stated that an exempt party forfeits its antitrust exemption whenever it acts in concert with nonexempt parties. *Id.*

84. *Id.* at 232-33.

85. 458 U.S. 119 (1982).

86. *Id.* at 129. In *Pireno*, the Court held that a health insurer's use of a professional association's peer review committee to examine chiropractic bills and render opinions was not the "business of insurance" under the Act, and that federal antitrust laws could be applied to the defendant's conduct. *Id.* at 134.

87. The Act has been criticized for at least two decades. See Weller, *supra* note 28, at 588 & n.11 (citing commentators advocating modification or repeal of the Act); U.S. DEPT. OF JUSTICE, *THE PRICING AND MARKETING OF INSURANCE* (1977); Laurence M. Hamric, Note, *The McCarran-Ferguson Act: A Time for Procompetitive Reform*, 29 VAND. L. REV. 1271, 1308 (1976) (concluding that insurance regulation under the Act has failed to protect consumers). For a thorough examination of the debate regarding the success and failure of the McCarran-Ferguson Act, see Achampong, *supra* note 46, at 141; Jay Angoff, *Insurance Against Competition: How the McCarran-Ferguson Act Raises Prices and Profits in the Property-Casualty Insurance Industry*, 5 YALE J. ON REG. 397 (1988); Melendez, *supra* note 28; William A. Montgomery, *Changing Insurance*

contend that the Act stifles competition in prices and insurance terms, which, in turn, results in higher premiums and a lack of policy options for consumers.⁸⁸ To some extent, lack of federal antitrust oversight assumes the existence of effective state regulation, which, critics argue, is often either nonexistent, ineffective, or a victim of regulatory “capture” by insurance companies.⁸⁹ Together, the antitrust exemption and the lack of effective state regulation has arguably resulted in a shortage of affordable liability insurance.⁹⁰ These concerns are likely to be the subject of continued debate in the wake of the Court’s recent *Hartford Fire Insurance* decision.⁹¹

A series of legislative proposals that would have either limited or repealed the McCarran-Ferguson Act received Congressional attention during the early 1990s,⁹² and even though none of these proposals was successful, Congress remains interested in regulatory reform of the insurance industry.⁹³ The proposed “Insurance Competitive

Policies: Coping with the New Antitrust Environment, 61 ANTITRUST L.J. 313 (1993); Nancy R. Page, Comment, *Risky Business: Consumer Protection in the Insurance Industry*, 23 HARV. J. ON LEGIS. 287 (1986); Kevin Thompson, *McCarran-Ferguson Repeal and ISO’s Advisory Rate Ban: A Chance for Compromise?* 17 N. KY. L. REV. 373 (1990).

88. See 137 CONG. REC. E38 (daily ed. Jan. 3, 1991) (statement of Rep. Brooks) (noting that “skyrocketing premiums and cutoffs in coverage are now an all too familiar experience in many Americans’ everyday lives” and that “the continuation of this special treatment for the insurance industry [under the McCarran-Ferguson Act] has become a proposition virtually impossible to defend”); see also Melendez, *supra* note 28, at 300 (discussing the Insurance Competitive Pricing Act of 1991, H.R. 9, 102d Cong., 1st Sess. (1991), a bill that was intended to modify the McCarran-Ferguson Act, and noting the remarks made by Rep. Brooks in support of the bill).

89. See Melendez, *supra* note 28, at 303-04 (outlining arguments by proponents for repeal of the Act). Regulatory capture is the phenomenon of a state agency being unduly influenced by the very interests being regulated. The regulated interests may, under these circumstances, use the regulatory mechanisms for their own purposes. See ALAN STONE, REGULATION AND ITS ALTERNATIVES 229-31 (1982) (describing the capture theory of regulatory politics).

90. Melendez, *supra* note 28, at 304.

91. 113 S. Ct. 2891 (1993). In *Hartford Fire Insurance*, the Court ruled on three principal issues: (1) whether insurers lose their McCarran-Ferguson Act immunity merely by acting in concert with nonexempt entities (in this case foreign insurers); (2) whether international comity requires American courts to decline jurisdiction over cases such as this; and (3) whether the insurers had engaged in a “boycott” as defined and used in the McCarran-Ferguson Act. *Id.* at 2901, 2908-11. The *Hartford Fire Insurance* case is discussed in detail *infra* part III.

92. See, e.g., The Insurance Competitive Pricing Act of 1991, H.R. 9, 102d Cong., 1st Sess. (1991). Such legislative proposals were deferred partially in anticipation of the *Hartford Fire Insurance* decision.

93. See Achampong, *supra* note 46, at 167-68; Montgomery, *supra* note 87, at 326-28 (discussing the Insurance Competitive Pricing Act of 1991 and the Federal Insurance Solvency Act of 1992).

Pricing Act of 1991"⁹⁴ ("H.R. 9") would have eliminated the exemption from the antitrust laws for four specific activities: (1) price fixing; (2) geographic market allocation; (3) tying arrangements; and (4) monopolization.⁹⁵ Joint collection of necessary historical and loss development data would have continued to receive an exemption,⁹⁶ and a later amendment would have permitted "small and medium-sized companies, with small market shares . . . to continue to share trending information used in determining insurance rates."⁹⁷

The National Association of Independent Insurers ("NAII") opposed H.R. 9 because it believed that the bill would result in litigation over the new provisions, force small insurers out of business, and drive premiums higher.⁹⁸ The NAIC similarly opposed H.R. 9 as did the American Insurance Association ("AIA").⁹⁹ The American Bar Association, however, endorsed the legislation.¹⁰⁰ Not surprisingly, the Bush Administration opposed H.R. 9 on the ground that the legislation would deter competitive collective action among insurers.¹⁰¹ H.R. 9 never reached the House floor, and the grant of certiorari in the *Hartford Fire Insurance* case slowed any further legislative efforts to revise the McCarran-Ferguson Act.¹⁰²

Another piece of proposed legislation, the "Federal Insurance Solvency Act of 1993,"¹⁰³ sponsored by Representative John Dingell, would limit federal oversight of the insurance industry by providing

94. H.R. 9, 102d Cong. 1st Sess. (1991).

95. See Montgomery, *supra* note 87, at 326; Margo D. Beller, *Brooks Reintroduces Bill to End Antitrust Immunity*, J. OF COM., Jan. 7, 1993, at 8A(1). A similar bill was proposed in the Senate, see S. 430, 102d Cong. 1st Sess. (1991), exempting virtually the same activities as H.R. 9. The primary distinction between H.R. 9 and S. 430 was a transition period in H.R. 9 providing an exemption for computing anticipated losses for future years. Montgomery, *supra* note 87, at 327 n.83.

96. See Montgomery, *supra* note 87, at 327.

97. Melendez, *supra* note 28, at 300 n.107.

98. *Id.* at 301.

99. *Id.* at 301-02. The AIA in fact attempted to reach a compromise with the House Judiciary Committee over antitrust provisions. See Editorial Comment, *AIA Did Right by McCarran*, NAT'L UNDERWRITER, June 29, 1992 at 28 (discussing AIA's attempts at compromise).

100. Melendez, *supra* note 28, at 303.

101. See Montgomery, *supra* note 87, at 327.

102. *Id.* It is unlikely that McCarran-Ferguson reform will rank high on the Congressional agenda in the near future, principally because Congress is so occupied with the issue of health insurance. See Mark A. Hofmann, *Insurer Regulation Bills on Back Burner: Little Action Seen on Dingell Plan, McCarran Reform*, BUS. INS., Feb. 22, 1993, at 3.

103. H.R. 1290, 103d Cong., 1st Sess. (1993). A previous version of this bill, H.R. 4900, was introduced in 1992 during the 102nd Congress. See H.R. REP. No. 417, 103d Cong., 2d Sess. 122-23 (1994).

property/casualty and life/health insurers the opportunity to obtain a "certificate of solvency" from a newly established Federal Insurance Solvency Commission, which would set solvency standards for both American and foreign insurers.¹⁰⁴ Under the proposed scheme, federally certified insurers would be exempt from state solvency regulations but would remain subject to state rate, form, and market conduct regulations, and would also be required to participate in state residual market mechanisms.¹⁰⁵ One commentator has noted, however, that a previous and very similar version of the Dingell Bill "threaten[ed] total confusion to insurance antitrust because it [was] silent as to how it would affect the application of the McCarran-Ferguson Act."¹⁰⁶

F. *Legal Doctrines Affecting Federal Regulation of Insurance*

In addition to the McCarran-Ferguson Act, there are two judicially created doctrines that affect the power of the federal government to regulate insurance in the United States. Both the state action doctrine and the consideration of international comity are well-established checks on the application of the federal antitrust laws, and both were raised by the defendants in *Hartford Fire Insurance*.

1. The "State Action" Doctrine

The so-called "state action" doctrine is a long-standing judicial exemption to the antitrust laws. Although courts have repeatedly stated that the Sherman Act is designed to foster competition, competition alone does not always result in sound economic policy.¹⁰⁷ As a result, the Supreme Court has determined that, in some instances, state legislatures may reasonably conclude that competition should be sacrificed in favor of regulation.¹⁰⁸ Thus, pursuant to the judicially created state action doctrine, states may determine that a particular industry or area of commerce requires some amount of regulation, and the state

104. See Montgomery, *supra* note 87, at 328.

105. *Id.* "Residual market mechanisms" include a variety of state schemes to make insurance available to all consumers. For example, a number of states provide an assigned risk pool into which auto insurance applicants, who cannot secure insurance otherwise, are placed. Insurance companies are required, as a condition of doing business in the state, to accept a certain percentage of these high-risk customers. Sometimes rates are set by the state as well. Similar schemes exist for homeowners' insurance and other property coverages.

106. *Id.* (commenting on H.R. 4900, 102d Cong., 2d Sess. (1992), a previous version of Representative Dingell's bill).

107. STEPHEN F. ROSS, PRINCIPLES OF ANTITRUST LAW 496-97 (1993).

108. See Parker v. Brown, 317 U.S. 341, 350-52 (1943).

may, by enactment of an appropriate regulatory scheme, displace federal antitrust regulation.¹⁰⁹

The Court first addressed the state action doctrine in *Parker v. Brown*.¹¹⁰ In *Parker*, a raisin producer challenged a California statute that restricted or allocated the production of certain agricultural products,¹¹¹ a scheme that would certainly be considered a conspiracy to restrain trade under the Sherman Act if put into effect solely by private parties.¹¹² Despite the relatively clear nature of the antitrust violation, the Court held that the Sherman Act was not intended to restrain activities directed by state legislatures.¹¹³ In other words, state legislatures may, by the adoption of appropriate regulatory schemes, restrict competition in a manner that private industries may not.¹¹⁴ The Court concluded that in adopting and enforcing its program, the State of California had neither entered into an agreement nor conspired to restrain trade with any party.¹¹⁵ Rather, California had imposed its program "as an act of government which the Sherman Act did not undertake to prohibit."¹¹⁶

While at first glance the Court's decision in *Parker v. Brown* appears to permit states to protect state business from federal antitrust regulation, the case has not been interpreted that broadly.¹¹⁷ In 1980, the Court issued one of its most important interpretations of the state

109. See Ross, *supra* note 107, at 496-99.

110. 317 U.S. 341 (1943).

111. *Id.* at 346.

112. *Id.* at 350.

113. *Id.* at 351.

114. The Court explained its reasoning:

[A] state does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful, and we have no question of the state or its municipality becoming a participant in a private agreement or combination by others for restraint of trade. Here the state command . . . is not rendered unlawful by the Sherman Act since, in view of the latter's words and history, it must be taken to be a prohibition of individual and not state action.

Parker, 317 U.S. at 351-52 (citations omitted).

115. *Id.*

116. *Id.* at 352.

117. See *Cantor v. Detroit Edison Co.*, 428 U.S. 579, 598 (1976) (concluding that a utility's anticompetitive conduct was not required by state law and therefore not immune from federal antitrust laws); *Goldfarb v. Virginia State Bar*, 421 U.S. 773, 790 (1975) (holding that for the state action exemption to apply, the acting party must show that a state law required the party to engage in the challenged activity); *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384, 388 (1951) (holding that a Louisiana statute enforcing a price-fixing agreement against both parties and nonparties to an agreement did not insulate a resale price maintenance scheme by whiskey and gin distributors from the federal antitrust laws).

action doctrine. In *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*,¹¹⁸ the Court addressed a Sherman Act challenge to a California statute that required all wine producers, wholesalers, and rectifiers to file fair trade contracts or price schedules with the state.¹¹⁹ In cases where a producer failed to enter into such a contract, wholesalers were required to post a price schedule for that producer's brands.¹²⁰ The statute prohibited state-licensed wine merchants from selling wine to retailers at any price other than one set in accordance with the statute.¹²¹

After observing that the system for wine pricing clearly constituted resale price maintenance in violation of the Sherman Act, the Court considered whether the state's involvement in the price setting program was sufficient to establish antitrust immunity under the state action doctrine.¹²² The Court declared that *Parker* and its progeny established two standards for antitrust immunity: (1) the restraint must be "clearly articulated and affirmatively expressed as state policy"; and (2) the State must actively supervise the challenged policy.¹²³ The Court determined that California had satisfied the first standard by forthrightly stating its legislative policy to permit resale price maintenance.¹²⁴ The Court concluded, however, that the California system did not satisfy the second standard, for the state had neither set the prices nor examined the reasonableness of the prices which were essentially set by private parties.¹²⁵ Rather, California merely authorized and enforced the price fixing.¹²⁶ Emphasizing that states cannot give immunity to those who violate the Sherman Act, the Court concluded that "[t]he national policy in favor of competition cannot be thwarted by casting such a gauzy cloak of state involvement over what is essentially a private price-fixing arrangement."¹²⁷

The Court reexamined the first prong of the *Midcal* test in *Southern*

118. 445 U.S. 97 (1980).

119. *Id.* at 99.

120. *Id.*

121. *Id.* The Court noted that the state did not have direct control over wine prices and did not review the reasonableness of the prices set by wine dealers. *Id.* at 99-100.

122. *Midcal*, 445 U.S. at 103.

123. *Id.* at 105 (quoting *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389, 410 (1978) (opinion of Brennan, J.)).

124. *Id.*

125. *Id.* The Court noted that California also failed to monitor market conditions and had never reevaluated the program. *Midcal*, 445 U.S. at 106.

126. *Id.* at 105.

127. *Id.* at 106.

Motor Carriers Rate Conference, Inc. v. United States.¹²⁸ In *Southern Motor Carriers*, four states had authorized rival trucking companies to agree on joint rates for intrastate trucking and then to file the rates for approval with the individual state regulatory commissions.¹²⁹ The issue confronting the Court was whether merely authorizing the truckers to agree satisfied *Midcal's* requirement of a clear expression of a state policy to displace competition with regulation.¹³⁰ The Court broadened *Midcal's* first prong, holding that so long as a state sufficiently articulates its intent to adopt legislation that permits anticompetitive conduct by regulated private parties, the first prong of the *Midcal* standard is satisfied.¹³¹ Thus, even though the states permitted rather than compelled anticompetitive behavior in *Southern Motor Carriers*, the Court concluded that the challenged conduct was immunized under *Parker v. Brown* because the state legislation either expressly approved the collective rate making or intentionally displaced competition by enacting price regulations.¹³²

The Court revisited the "active supervision" prong of the *Midcal* test in *Patrick v. Burget*.¹³³ In *Patrick*, a surgeon brought an antitrust action against several physician members of a peer-review committee, established pursuant to Oregon law, that had terminated the surgeon's staff privileges.¹³⁴ Despite the state's involvement in creating the peer-review system, the Supreme Court held that the revocation was a private decision not actively supervised by the state.¹³⁵ According to the Court, the active supervision requirement ensures that "the state-action doctrine will shelter only the particular anticompetitive acts of private parties that, in the judgment of the State, actually further state regulatory policies."¹³⁶ Therefore, *Midcal's* second prong is satisfied only where state officials have and exercise the power to review and approve particular anticompetitive acts of private parties.¹³⁷

The Court further refined the active supervision requirement in *FTC v. Ticor Title Insurance Co.*¹³⁸ In *Ticor*, the Federal Trade

128. 471 U.S. 48 (1985).

129. *Id.* at 50.

130. *Id.* at 55.

131. *Id.* at 60.

132. *Id.* at 58-65.

133. 486 U.S. 94 (1988).

134. *Id.* at 96-97.

135. *Id.* at 105.

136. *Id.* at 101 (citation omitted).

137. *Id.*

138. 112 S. Ct. 2169 (1992). The case is particularly relevant to *Hartford Fire Insurance* because it also concerns the application of the antitrust laws to the insurance

Commission ("FTC") filed a complaint charging several title insurance companies in four states with horizontal price-fixing by setting fees for title searches and examinations in violation of the Federal Trade Commission Act.¹³⁹ State-licensed rating bureaus established uniform rates and filed them with their respective states, each of which used a "negative option" system to approve rate filings.¹⁴⁰ Under this system, rates filed by the rating bureaus became effective unless the State rejected them within a specified period of time, usually 30 days.¹⁴¹ The Administrative Law Judge ("ALJ") determined that this particular negative option system imposed only "minimal scrutiny" by state regulators.¹⁴² Accordingly, even though the FTC conceded on review of the ALJ's decision that the first part of the *Midcal* standard—the articulation of a clear policy to permit anticompetitive conduct—had been satisfied, it determined that the second prong, which requires active state supervision, had not been satisfied in any of the four states.¹⁴³

The *Ticor* Court traced the history of the *Midcal* standards and considered first whether "principles of federalism" justified a broad interpretation of state action immunity.¹⁴⁴ The Court found a "powerful refutation" of that argument because thirty-six states filed briefs as *amici curiae* opposing a broad immunity rule.¹⁴⁵ The Court agreed with the *amici* states and held that state action immunity arises only where there is "real compliance with both parts of the *Midcal* test."¹⁴⁶ The Court rejected a more formalistic but less demanding

industry, and its holding may have in fact induced ISO to abandon its practice of filing rates before state insurance departments.

139. *Id.* at 2172.

140. *Id.* at 2174.

141. *Id.*

142. *Ticor*, 112 S. Ct. at 2174. The ALJ rejected the McCarran-Ferguson defense, and the Court did not question those determinations. *Id.*

143. *Id.* at 2175-76.

144. *Id.* at 2178.

145. *Id.*

146. *Ticor*, 112 S. Ct. at 2178. The Court explained why it agreed with the narrower interpretation of the *Midcal* test advanced by the states:

If the States must act in the shadow of state-action immunity whenever they enter the realm of economic regulation, then our doctrine will impede their freedom of action, not advance it. . . . By adhering in most cases to fundamental and accepted assumptions about the benefits of competition within the framework of the antitrust laws, we increase the States' regulatory flexibility. . . . Neither federalism nor political responsibility is well served by a rule that essential national policies are displaced by state regulations intended to achieve more limited ends. For States which do choose to displace the free market with regulation, our insistence on real compliance with both parts of

view of the “active supervision” rule enunciated by another court,¹⁴⁷ stating that a “mere potential for state supervision is not an adequate substitute for a decision by the State.”¹⁴⁸ Applying this more stringent standard, the Court determined that although the state schemes provided the *potential* for state supervision, that potential “was not realized in fact.”¹⁴⁹ Accordingly, the Court concluded that the “active supervision” prong of *Midcal* was not satisfied, and that the title insurance companies were not entitled to immunity from the federal antitrust laws under the state action doctrine.¹⁵⁰

In a concurring opinion, Justice Scalia commented that even though the Court’s standard for “active supervision” would create uncertainty for states, he saw no alternative.¹⁵¹ Noting that the active supervision doctrine itself had not been challenged, Justice Scalia expressed his skepticism toward the *Parker v. Brown* exemption, which he characterized as permitting “state-programmed private collusion.”¹⁵² In dissent, Chief Justice Rehnquist, joined by Justices O’Connor and Thomas, claimed that the majority’s decision would require courts to make normative judgments about whether a state’s regulatory scheme is “sufficiently active.”¹⁵³ Justice O’Connor, joined by Justice Thomas, filed a separate dissent, contending that the decision would unfairly burden state regulators and would probably eliminate the use of negative option regulations.¹⁵⁴

The state action doctrine is at best a complicating factor in the

the *Midcal* test will serve to make clear that the State is responsible for the price fixing it has sanctioned and undertaken to control. . . . For States whose object it is to benefit their citizens through regulation, a broad doctrine of state-action immunity may serve as nothing more than an attractive nuisance in the economic sphere.

Id.

147. *See* *New England Motor Rate Bureau, Inc. v. FTC*, 908 F.2d 1064, 1071 (1st Cir. 1990) (holding that the state action doctrine is satisfied “[w]here . . . the State’s program is in place, is staffed and funded, grants to State officials ample power and the duty to regulate pursuant to declared standards of state policy, is enforceable in the State’s courts, and demonstrates some basic level of activity directed towards seeing that the private actors carry out the State’s policy and not simply their own policy”).

148. *Ticor*, 112 S. Ct. at 2179.

149. *Id.*

150. *Id.* at 2180. The *Ticor* Court distinguished the “negative option” scheme approved in *Southern Motor Carriers* because, in that case, the government conceded that the active supervision requirement had been met through regularly held hearings that used the industry submissions as a starting point. *Id.* at 2179-80.

151. *Ticor*, 112 S. Ct. at 2180-81 (Scalia, J., concurring).

152. *Id.* at 2181 (Scalia, J., concurring).

153. *Id.* at 2182-83 (Rehnquist, C.J., dissenting).

154. *Id.* at 2183-84 (O’Connor, J., dissenting). Neither dissent considered the point that 36 states had filed briefs as *amici curiae* requesting *narrower* immunity.

regulation of the insurance industry. Though modified in *Ticor*, this doctrine provides another limitation on the use of antitrust laws to regulate the insurance industry. Indeed, under the state action doctrine, states may be able to displace the effect of the antitrust laws in insurance regulation, even in the absence of the McCarran-Ferguson Act.

At least one commentator has observed an intimate relationship between the state action doctrine and the McCarran-Ferguson Act,¹⁵⁵ and even though the legislative history of the Act is quite clear in stating that it was intended to “enunciate” the *Parker* doctrine,¹⁵⁶ only one court has adopted that view.¹⁵⁷

2. The Principle of International Comity

Courts have created a second doctrine that limits the effect of the federal antitrust laws upon the insurance industry. Under the principle of international comity, even if a court determines that it has subject matter jurisdiction over an action against a foreign insurance company, international comity may bar the exercise of that jurisdiction.¹⁵⁸ This doctrine reflects the understanding that although the Sherman Act may encompass the foreign activities of aliens as well as American citizens, it may not be appropriate for federal courts to exercise their jurisdiction in all situations.¹⁵⁹ Extraterritorial application of the antitrust laws, or any laws for that matter, have the potential for causing international resentment and protest, as well as undermining vital national interests abroad.¹⁶⁰ In *Timberlane Lumber Co. v. Bank of America, N.T. & S.A.*,¹⁶¹ the Ninth Circuit articulated the principles underlying the

155. See Weller, *supra* note 28, at 615-19.

156. See *id.* at 617.

157. See *Allstate Ins. Co. v. Lanier*, 242 F. Supp. 73, 87 (E.D.N.C. 1965) (noting that “Section 2(b) was written into the [McCarran-Ferguson] Act as an enunciation of the *Parker v. Brown* decision”), *cert. denied*, 385 U.S. 930 (1966); see also Weller, *supra* note 28, at 617 n.147 (stating that the state action doctrine and the McCarran-Ferguson Act are intimately related).

158. See *In re Insurance Antitrust Litig.*, 723 F. Supp. 464, 487 (N.D. Cal. 1989); see also *In re Insurance Antitrust Litig.*, 938 F.2d 919, 932 (9th Cir. 1991) (noting that although the Foreign Trade Antitrust Improvements Act of 1982 (“FTAIA”) does not eliminate the defense of international comity, “it is only in an unusual case that comity will require abstention from the exercise of jurisdiction”).

159. See *Timberlane Lumber Co. v. Bank of America, N.T. & S.A.*, 549 F.2d 597, 608-09 (9th Cir. 1976).

160. *Id.* at 609; see *Laker Airways Ltd. v. Sabena, Belgian World Airlines*, 731 F.2d 909, 937 (D.C. Cir. 1984) (“[W]hen possible, the decisions of foreign tribunals should be given effect in domestic courts, since recognition fosters international cooperation and encourages reciprocity, thereby promoting predictability and stability.”).

161. 549 F.2d 597 (9th Cir. 1976).

doctrine of international comity:

[T]he antitrust laws require in the first instance that there be *some* effect—actual or intended—on American foreign commerce before the federal courts may legitimately exercise subject matter jurisdiction under [the federal antitrust] statutes. Second, a greater showing of burden or restraint may be necessary to demonstrate that the effect is sufficiently large to present a cognizable injury to the plaintiffs and, therefore, a civil *violation* of the antitrust laws. Third, there is the additional question which is unique to the international setting of whether the interests of, and links to, the United States—including the magnitude of the effect on American foreign commerce—are sufficiently strong, *vis-à-vis* those of other nations, to justify an assertion of extraterritorial authority.¹⁶²

The *Timberlane* court then adopted a “jurisdictional rule of reason” and weighed several factors to determine whether, as a matter of international comity and fairness, it should exercise extraterritorial jurisdiction.¹⁶³ Those factors include:

[T]he degree of conflict with foreign law or policy, the nationality or allegiance of the parties and the locations or principal places of business of corporations, the extent to which enforcement by either state can be expected to achieve compliance, the relative significance of effects on the United States as compared with those elsewhere, the extent to which there is explicit purpose to harm or affect American commerce, the foreseeability of such effect, and the relative importance to the violations charged of conduct within the United States as compared with conduct abroad.¹⁶⁴

Although the oft quoted *Timberlane* test “has commanded a strong

162. *Id.* at 613 (footnote omitted). The *Timberlane* court based its analysis on the act of state doctrine discussed in *Underhill v. Hernandez*, 168 U.S. 250, 252 (1897), which held that “[e]very sovereign State is bound to respect the independence of every other sovereign State, and the courts of one country will not sit in judgment on the acts of the government of another done within its own territory.” See *Timberlane*, 549 F.2d at 605. The *Timberlane* court also considered the act of state doctrine as stated in *Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398, 440 (1964) (noting that where American courts face the question of whether to exercise jurisdiction over acts in a foreign jurisdiction, there is a potential for interference with the conduct of foreign affairs by other branches of the government, and the jurisdictional decision must be based upon “the balance of considerations”); and *American Banana Co. v. United Fruit Co.*, 213 U.S. 347, 357 (1909) (stating that “[t]he foregoing considerations would lead in case of doubt to a construction of any statute as intended to be confined in its operation and effect to the territorial limits over which the lawmaker has general and legitimate power”). See *Timberlane*, 549 F.2d at 605-06.

163. *Id.* at 613.

164. *Id.* at 614.

following,"¹⁶⁵ federal courts have not applied it consistently,¹⁶⁶ and as the Supreme Court's five-to-four split in *Hartford Fire Insurance* suggests, it remains a complex issue in the realm of insurance regulation in this country.

III. STEMMING THE TIDE OF FEDERAL AUTHORITY: *HARTFORD FIRE INSURANCE CO. V. CALIFORNIA*

The half-century of experience with the McCarran-Ferguson Act and the related state action and comity doctrines culminated in 1993, in what was broadly anticipated to be one of the most important cases involving insurance regulation ever to be filed. The case promised (or threatened) to resolve many of the past questions that had clouded antitrust enforcement against insurance companies. While the case promised some long-needed answers, the promises remained largely unfulfilled. The answers provided by the Supreme Court were murky and complex, involving two majority opinions on two different issues. In many ways, the decision exemplifies the confused state of the law that has arisen under the McCarran-Ferguson Act, and thus illustrates the need for a fresh start.

A. *The Facts and Procedural History of the Hartford Fire Insurance Litigation*

The *Hartford Fire Insurance* litigation began with a series of actions brought by nineteen states, as *parens patriae* actions, and numerous private plaintiffs against a group of insurance companies, reinsurance

165. 1 JAMES R. ATWOOD & KINGMAN BREWSTER, ANTITRUST AND AMERICAN BUSINESS ABROAD § 6.11, at 162 (2d ed. 1981), *quoted in Insurance Antitrust Litig.*, 938 F.2d at 932. The Third Circuit, for example, elaborated on the *Timberlane* opinion in formulating a ten-part test that considers: (1) the extent of any conflict with foreign law or policy; (2) the nationality of both parties; (3) the relative importance of the alleged violation in the United States compared to that abroad; (4) the availability of a remedy or pending litigation abroad; (5) the existence of intent to harm or affect American commerce and the foreseeability of that harm; (6) the impact upon foreign relations if the court exercises its jurisdiction and grants relief; (7) whether a party will be forced to perform an act that may be illegal in either country or will be subject to conflicting requirements if the court grants relief; (8) whether the court can effectively enforce its order; (9) whether the court's resolution of the controversy would be acceptable in this country if made by a foreign nation under similar circumstances; and (10) whether any treaty between the United States and the pertinent nations addresses the issue. *See Mannington Mills, Inc. v. Congoleum Corp.*, 595 F.2d 1287, 1297-98 (3d Cir. 1979); *see also* ATWOOD & BREWSTER, *supra*, at 162 & n.109 (discussing the Third Circuit's application of the *Timberlane* factors in *Mannington Mills*).

166. *See, e.g., infra* part III.C.1, discussing the various approaches taken by the district court, the Ninth Circuit, and the Supreme Court in the *Hartford Fire Insurance* litigation in applying the *Timberlane* test.

companies, underwriters, brokers, individuals, and the Insurance Services Office (“ISO”), alleging numerous violations of the federal antitrust laws.¹⁶⁷ The litigation primarily focused on coverage under commercial general liability (“CGL”) insurance and property insurance.¹⁶⁸

In *Hartford Fire Insurance*, the plaintiffs alleged that the defendant primary insurers, reinsurers, retrocessional insurers, and ISO engaged in several illegal conspiracies to restrict the terms of coverage of CGL insurance in violation of section 1 of the Sherman Act.¹⁶⁹ The events that culminated in the alleged antitrust violations commenced in 1984, when ISO filed two proposed new policy forms for CGL insurance that substantially modified its previous policy forms.¹⁷⁰ One of the proposed forms contained a traditional “occurrence-based” trigger,

167. See *In re Insurance Antitrust Litig.*, 723 F. Supp. 464, 468 (N.D. Cal. 1989).

168. *Id.* Typically, businesses, nonprofit organizations, and governmental entities purchase CGL insurance as protection against liability claims of third parties for bodily injury or property damage. These entities often purchase CGL coverage from *primary insurers* such as the defendants Hartford Fire Insurance Co., Allstate Insurance Co., Aetna Casualty and Surety Co., and the CIGNA Corp., which are some of the nation’s major providers of CGL insurance. *Id.* Primary insurers likewise share their risks with *reinsurers*, and reinsurers in turn share their risks with *retrocessional* insurers, who essentially provide insurance for reinsurers. *In re Insurance Antitrust Litig.*, 938 F.2d 919, 922 (9th Cir. 1991). Reinsurance policies, commonly arranged by specialized brokers and underwriters, are often written by syndicates doing business through Lloyd’s of London. *Id.* at 923. The arrangements between the primary insurer, the reinsurer, and the retrocessional insurer can all affect the terms and availability of primary insurance. *Id.* at 922. For example, the ability of a primary insurer to obtain reinsurance bears a direct impact on the willingness and ability of the primary insurer to provide insurance to businesses and other entities. See *Insurance Antitrust Litig.*, 723 F. Supp. at 473. In the *Hartford Fire Insurance* case, among the defendant reinsurers were both domestic and foreign insurers, including one Swiss corporation and six London company market corporations, all of which are subsidiaries of American corporations. *Insurance Antitrust Litig.*, 938 F.2d at 922-23.

Commercial general liability policies are written predominately on standardized policy forms developed by defendant ISO, an organization of 1400 property and casualty insurers—including defendants Hartford, Allstate, Aetna, and CIGNA—that is licensed as a rating service and advisory organization in all fifty states. *Insurance Antitrust Litig.*, 723 F. Supp. at 468. ISO prepares standardized policy forms and files them with state insurance departments and also performs other services for primary insurers such as providing loss data, projecting future loss trends, and calculating advisory rates. *Id.* at 468-69. Most importantly, however, ISO is the “almost exclusive source of support services in this country for CGL insurance.” *Hartford Fire Ins. Co. v. California*, 113 S. Ct. 2891, 2896 (1993) (citation omitted).

169. *Id.* at 2895. Plaintiffs specifically claimed that the defendant insurers conspired to affect several markets for insurance including the U.S. markets for CGL insurance, excess and umbrella CGL insurance, property insurance, the reinsurance markets in both the U.S. and the U.K., and the retrocessional insurance market in the U.K. *Insurance Antitrust Litig.*, 938 F.2d at 924.

170. *Hartford Fire Insurance*, 113 S. Ct. at 2897.

under which an insured would be covered for any claims arising out of occurrences during the policy period, regardless of when the claim was asserted.¹⁷¹ Under an occurrence-based form, insurers risk exposure to so-called “long-tail” risks that could arise long after the policy period ends.¹⁷² The other proposed form included a “claims-made” trigger under which coverage would be limited to claims actually *made* during the policy period.¹⁷³ The claims-made form, however, did not contain a retroactive-date provision.¹⁷⁴ Consequently, even under the claims-made form, insurers would remain potentially liable for unknown claims that could arise under previous policy provisions.¹⁷⁵ Both of the proposed forms provided coverage for “sudden and accidental pollution” damage as well as unlimited coverage of legal defense costs.¹⁷⁶

Several of the defendant insurers objected to the proposed CGL forms, particularly the retention of the occurrence-based form, the lack of a retroactive-date provision on the claims-made form, and the inclusion in both forms of the environmental and legal costs provisions.¹⁷⁷ Majorities in ISO subcommittees, however, supported the proposed 1984 forms without any of the modifications desired by the defendant insurers, and in December 1983, the ISO Board of Directors approved the proposed forms and filed the forms with state regulators in March of 1984.¹⁷⁸

Dissatisfied with the adoption of the proposed CGL forms by ISO, the defendant primary insurers, reinsurers, and retrocessional insurers allegedly conspired to manipulate the standard CGL policies and to compel other primary insurers to similarly modify their standard CGL forms to conform with the particular policies that the defendant insurers wished to sell.¹⁷⁹ Although the plaintiffs claim that the defen-

171. *Id.*

172. *See Insurance Antitrust Litig.*, 938 F.2d at 923.

173. *Hartford Fire Insurance*, 113 S. Ct. at 2896, 2897.

174. *Id.* at 2897. A “retroactive-date provision” restricts coverage even further than a claims-made policy, by obligating the insurer to cover only those claims that are based upon incidents that occur after a certain date specified in the policy. *Id.* at 2896. Describing the benefit of a retroactive-date provision in a claims-made policy, the Supreme Court noted that “[s]uch a provision eliminates the risk that an issuer, by issuing a claims-made policy, would assume liability arising from incidents that occurred before the policy’s effective date, but remained undiscovered or caused no immediate harm.” *Id.*

175. *See id.*

176. *Hartford Fire Insurance*, 113 S. Ct. at 2897.

177. *Id.*

178. *Id.*

179. *Id.* at 2897-99.

dant insurers engaged in several conspiracies in numerous combinations, the alleged conspirators essentially sought to secure four changes in the proposed ISO forms: (1) the replacement of occurrence-based coverage with claims-made coverage; (2) the insertion of a retroactive-date provision, restricting coverage to claims based on incidents that occurred after a certain date; (3) the elimination of coverage for "sudden and accidental" pollution; and (4) the insertion of a provision that would place a cap on legal defense costs.¹⁸⁰

According to the complaints, the defendant primary insurers engaged in a concerted effort to manipulate and restrict the terms of ISO standard CGL forms. The defendants' alleged conspiracy began in June 1984, when defendant Hartford allegedly persuaded major reinsurers to agree to boycott the ISO form unless ISO added a retroactive-date provision to its "claims-made" forms.¹⁸¹ Defendants Hartford, Aetna, Allstate, and CIGNA also allegedly acted together to successfully persuade key London underwriters at Lloyd's to agree to boycott the ISO forms, using reinsurance brokers to convey their message.¹⁸² Indeed, lead underwriters at Lloyd's themselves allegedly met representatives of ISO in London on July 4, 1984 and expressed their desire to eliminate the occurrence form.¹⁸³ Four reinsurance underwriters from Lloyd's then allegedly attended an ISO executive committee meeting in September 1984, during which they insisted that defendant Hartford's terms be included in the CGL form, effectively telling ISO that it must "[c]hange the form or get no reinsurance."¹⁸⁴ According to the plaintiffs, ISO subsequently gave in to these demands, eliminating accidental pollution coverage and approving a claims-made form with a retroactive-date provision.¹⁸⁵

The reinsurers allegedly continued to pressure ISO to eliminate the

180. *Hartford Fire Insurance*, 113 S. Ct. at 2897-99. Two important features of the insurance industry may have helped to facilitate the defendant insurers' ability to exert pressure on other primary insurers and to obtain their desired changes to the CGL forms. First, most primary insurers rely on outside support services to provide the coverage that they sell, and the defendant ISO is essentially the exclusive provider of such support services in this country. See *supra* text accompanying notes 22-26 and note 168. Second, most primary insurers must acquire insurance from reinsurers to cover a portion of their risk. See *supra* note 168. Hence, by cooperation with or control over ISO and major reinsurers, the defendant insurers could effectively compel other primary insurers to conform their policies to the particular policies that the defendant insurers wanted to sell.

181. *Insurance Antitrust Litig.*, 938 F.2d at 923.

182. *Id.*

183. *Id.* at 929.

184. *Id.* at 923.

185. *Insurance Antitrust Litig.*, 938 F.2d at 923. ISO, however, continued to offer an occurrence-based form. *Id.*

occurrence-based form and also began to promote the new claims-made forms by announcing publicly that they would not provide reinsurance for any primary insurers writing policies based on the occurrence form.¹⁸⁶ Moreover, the plaintiffs claimed, the reinsurers “refused to renew long-standing reinsurance treaties with primary insurers in the United States unless they agreed to abandon the occurrence form.”¹⁸⁷

In late 1985, the defendant insurers also allegedly conspired to restrain trade in the market for excess and umbrella insurance by pressuring ISO to approve standard excess and umbrella CGL forms, which are normally not offered on a regulated basis.¹⁸⁸ ISO subsequently approved the proposed excess and umbrella policy forms, which contained a retroactive-date provision in “claims-made” policies and a pollution exclusion and cap on defense costs in both “claims-made” and “occurrence” policies.¹⁸⁹

Finally, the plaintiffs claimed that London retrocessional reinsurers agreed in 1987 to boycott reinsurance and insurance policies for U.S. property seepage and pollution exposures.¹⁹⁰ As evidence of the alleged boycott, plaintiffs pointed to the “Non-Marine London Market Agreement 1987,” a document signed by over forty London retrocessional reinsurers that effectively denied U.S. customers primary insurance coverage for seepage and pollution.¹⁹¹

Defendants filed five motions to dismiss or, in the alternative, for summary judgment, contending, *inter alia*, that they were entitled to antitrust immunity under the McCarran-Ferguson Act.¹⁹² The district

186. *Id.*

187. *Id.*

188. *Insurance Antitrust Litig.*, 938 F.2d at 924; see *Hartford Fire Insurance*, 113 S. Ct. at 2899.

189. *Hartford Fire Insurance*, 113 S. Ct. at 2899.

190. *Insurance Antitrust Litig.*, 938 F.2d at 924.

191. *Id.* The signatories agreed that they would only write retrocessional reinsurance policies if reinsurers signed a letter stating that:

We hereby agree that we will use our best endeavors to ensure that all U.S.A. and Canadian exposed insurance/reinsurance business attaching on or after 1st January 1987 will only be written where the original business includes a seepage and pollution exclusion clause wherever legal and applicable.

Id.

192. *Insurance Antitrust Litig.*, 723 F. Supp. at 471. The other defenses that the defendants raised included: (1) exemption under the state action immunity doctrine; (2) lack of standing; (3) lack of any factual allegation linking the foreign reinsurer defendants to a global conspiracy; and (4) lack of subject matter jurisdiction and international comity. *Id.* at 471-72. The foreign reinsurer and retrocessional reinsurer defendants and one broker also moved to dismiss the two claims alleging conspiracies to eliminate pollution coverage. *Id.* at 471.

court granted the defendants motion,¹⁹³ but the Court of Appeals for the Ninth Circuit reversed.¹⁹⁴ The Supreme Court granted the defendants' petition for a writ of certiorari on three issues, including "[w]hether agreements among primary insurers and reinsurers on such matters as standardized advisory insurance policy forms and terms of insurance coverage constitute a 'boycott' outside the exemption of the McCarran-Ferguson Act."¹⁹⁵

B. Application of the McCarran-Ferguson Act to the Hartford Fire Insurance Case

All three courts in *Hartford Fire Insurance* agreed that determining whether McCarran-Ferguson Act immunity applies to certain conduct involves a three-step analysis. First, the court must examine whether the pertinent conduct is within the scope of the "business of insurance."¹⁹⁶ The court then must determine whether that business is regulated by the states.¹⁹⁷ Finally, the court must determine whether the conduct at issue involves "boycott, coercion or intimidation."¹⁹⁸

1. The "Business of Insurance"

In *Insurance Antitrust Litigation* (as *Hartford Fire Insurance* was captioned in the lower courts), the plaintiffs took the position that the McCarran-Ferguson antitrust exemption for the insurance industry did not extend to the reinsurers or retrocessional insurers because, under the reasoning of *Union Labor Life Insurance Co. v. Pireno*,¹⁹⁹ the

193. See *Insurance Antitrust Litig.*, 938 F.2d at 925. The court of appeals characterized the district court's action as a dismissal for failure to state a cause of action or, in the alternative, as summary judgment for the defendants. *Id.*

194. *Id.* at 934.

195. *Hartford Fire Insurance*, 113 S. Ct. at 2900 n.8 (citation omitted). The Court granted certiorari to consider two other questions: "1. Whether domestic insurance companies whose conduct otherwise would be exempt from the federal antitrust laws under the McCarran-Ferguson Act lose that exemption because they participate with foreign reinsurers in the business of insurance"; and "2. Whether agreements among primary insurers and reinsurers on such matters as standardized advisory insurance policy forms and terms of insurance coverage constitute a 'boycott' outside of the McCarran-Ferguson Act." *Id.*

196. See *Hartford Fire Insurance v. California*, 113 S. Ct. 2891, 2901 (1993); *Insurance Antitrust Litig.*, 938 F.2d at 927; *Insurance Antitrust Litig.*, 723 F. Supp. at 473.

197. See *Hartford Fire Insurance*, 113 S. Ct. at 2902; *Insurance Antitrust Litig.*, 938 F.2d at 931; *Insurance Antitrust Litig.*, 723 F. Supp. at 473.

198. See *Hartford Fire Insurance*, 113 S. Ct. at 2901; *Insurance Antitrust Litig.*, 938 F.2d at 928; *Insurance Antitrust Litig.*, 723 F. Supp. at 473.

199. 458 U.S. 119 (1982). In *Pireno*, the Supreme Court established specific criteria for determining what constitutes the "business of insurance." See *supra* notes 85-86 and

“business of insurance” does not include reinsurance.²⁰⁰ In support of this argument, the plaintiffs contended that reinsurance only indirectly relates to risk-spreading and that it is not integral to the policy relationship between the insurer and insured.²⁰¹ The district court disagreed with the plaintiffs, and it held that at all levels, the activities of the defendants involved the “business of insurance,” including primary, excess or umbrella insurance, reinsurance, and retrocessional insurance.²⁰² The court concluded that the plaintiffs’ argument was an unreasonably narrow application of the language in *Pireno* and that reinsurance was indeed “an integral and vital part of the business of insurance.”²⁰³ The court noted that its conclusion was consistent with the plaintiffs’ characterization of reinsurance as a vital component of the insurance industry in their complaints.²⁰⁴

Although, in the words of the Ninth Circuit, the plaintiffs did not “seriously argue” on appeal that the foreign reinsurance contracts did not constitute the “business of insurance,” this issue found its way into the Supreme Court’s opinion in another context. In the Ninth Circuit, the plaintiffs argued that even though reinsurance and retrocessional insurance activities constituted the “business of insurance” and were normally exempt from federal antitrust laws, the defendant insurers had forfeited their McCarran-Ferguson Act exemption.²⁰⁵ The Ninth Circuit agreed, concluding that under the Supreme Court’s reasoning in *Group Life & Health Insurance Co. v. Royal Drug Co.*,²⁰⁶ the domestic defendants lost their McCarran-Ferguson immunity when they conspired with the nonexempt foreign defendants.²⁰⁷

The Supreme Court did not address whether the foreign reinsurers were subject to state regulation.²⁰⁸ Instead, in the only unanimous part

accompanying text.

200. *Insurance Antitrust Litig.*, 723 F. Supp. at 473. It was undisputed that the defendant insurers’ activities pertaining to the terms and conditions of primary, excess, and umbrella coverage involved the “business of insurance.” *Id.*

201. *Id.*

202. *Insurance Antitrust Litig.*, 723 F. Supp. at 473-74.

203. *Id.* at 473.

204. *Id.* The court also noted that the legislative history of the McCarran-Ferguson Act referred to reinsurance. *Id.* (citing 90 Cong. Rec. A4406 (1944) and 89 Cong. Rec. 6528 (1943)).

205. *Insurance Antitrust Litig.*, 938 F.2d at 928.

206. 440 U.S. 205 (1979). For a discussion of the Supreme Court’s *Royal Drug* decision, see *supra* notes 71-84 and accompanying text.

207. *Insurance Antitrust Litig.*, 938 F.2d at 928 (citing *Royal Drug*, 440 U.S. at 231).

208. For the Ninth Circuit’s discussion of this issue, see *Insurance Antitrust Litig.*, 938 F.2d at 928.

of its decision, the Court stated that the Ninth Circuit's interpretation of *Royal Drug* was in error.²⁰⁹ Writing for the Court, Justice Souter reasoned that the court of appeals' reliance upon *Royal Drug* was based on a faulty analogy and concluded that the court of appeals was incorrect in holding that the defendant domestic insurers had forfeited their McCarran-Ferguson exemption "simply because they agreed or acted with foreign reinsurers that . . . were 'not regulated by State Law.'"²¹⁰

One particular passage in the Court's opinion in *Royal Drug* supplied the source of controversy between the Supreme Court and the court of appeals in the *Hartford Fire Insurance* case:

Application of [the principle that antitrust exemptions are to be narrowly construed] is particularly appropriate in this case because the Pharmacy Agreements involve parties wholly outside the insurance industry. *In analogous contexts, the Court has held that an exempt entity forfeits antitrust exemption by acting in concert with nonexempt parties.* The Court has held, for example, that an exempt agricultural cooperative under the Capper-Volstead Act loses its exemption if it conspires with nonexempt parties.²¹¹

In the *Hartford Fire Insurance* case, the court of appeals grasped onto the language quoted above as precedent for its decision that as a rule, an exempt party forfeits its exemption by conspiring with a nonexempt party.²¹² The Supreme Court, however, characterized the *Royal Drug* passage as a "rough analogy" because the examples cited there concerned the Capper-Volstead Act, which exempts entities rather than activities.²¹³ In contrast, the Court suggested, the

209. See *Hartford Fire Insurance*, 113 S. Ct. at 2903.

210. *Hartford Fire Insurance*, 113 S. Ct. at 2903 (quoting *Insurance Antitrust Litig.*, 938 F.2d at 928) (footnote omitted). The Court refused to express an opinion as to whether state law regulated the activities of either the domestic or foreign reinsurers, leaving that question to the court of appeals on remand. *Id.* at 2903 n.12.

211. *Royal Drug*, 440 U.S. at 231 (emphasis added) (footnotes and citations omitted). Applying this principle to the Blue Shield Pharmacy Agreements, the Court further commented on the narrowness of the exemption:

If agreements between an insurer and retail pharmacists are the "business of insurance" because they reduce the insurer's costs, then so are all other agreements insurers may make to keep their costs under control—whether with automobile body repair shops or landlords. Such agreements would be exempt from the antitrust laws if Congress had extended the coverage of the McCarran-Ferguson Act to the "business of insurance companies." But that is precisely what Congress did not do.

Id. at 232-33 (footnote omitted).

212. See *Insurance Antitrust Litig.*, 938 F.2d at 928.

213. *Hartford Fire Insurance*, 113 S. Ct. at 2902.

McCarran-Ferguson Act only exempts *activities* inherent in the business of insurance, and not the mere status of being an insurer.²¹⁴

Within this context, the Supreme Court concluded that the agreements in *Hartford Fire Insurance* differed from the agreements in *Royal Drug*.²¹⁵ The Court noted that agreements made by insurance companies with entities outside the insurance industry, such as Blue Shield's agreements with pharmacies, "are unlikely to be about anything that could be called 'the business of insurance.'"²¹⁶ The Court opined that such transactions may constitute the "business of insurance *companies*," but they do not involve the "business of insurance" within the meaning of the Act.²¹⁷ Applying these principles to the facts of *Hartford Fire Insurance*, the Court noted that the defendants allegedly conspired with participants in the insurance industry, and concluded that their agreements did involve the "business of insurance."²¹⁸ Thus, because the McCarran-Ferguson Act exempts activities, not particular entities, the Court held that the defendant insurers did not lose their antitrust immunity by acting in concert with nonexempt entities; rather, the defendant insurers qualified for the antitrust exemption under the Act because their alleged activities were within the scope of the "business of insurance."

2. Division of Authority Between the States and the Federal Government

Under the McCarran-Ferguson Act, the federal antitrust laws can only apply to the business of insurance "to the extent that such business is not regulated by State Law."²¹⁹ Although the plaintiffs argued that the defendants' business activities were not regulated by state law and thus not exempted from the federal antitrust laws under McCarran-Ferguson, the plaintiffs alleged in their complaints that the defendants had violated state laws in addition to federal antitrust laws.²²⁰ Noting the rather substantial regulatory schemes of each of

214. The Court's opinions in *Hartford Fire Insurance*, 113 S. Ct. at 2891, *Royal Drug*, 440 U.S. at 205, *National Securities*, 393 U.S. at 453, and *SEC v. Variable Annuity Life Ins. Co.*, 359 U.S. 65 (1959), present a line of cases that suggest that a defendant's activities are more important than the type of entity the defendant is in determining whether it is exempt from the antitrust laws under the McCarran-Ferguson Act.

215. *Hartford Fire Insurance*, 113 S. Ct. at 2902.

216. *Id.* (quoting *Royal Drug*, 440 U.S. at 233).

217. *Id.*

218. *Id.* The Court further noted that it was undisputed that the alleged conspiracies fell within the scope of the "business of insurance." *Id.*

219. 15 U.S.C. § 1012(b) (1988); see *supra* note 32 and accompanying text.

220. *Insurance Antitrust Litig.*, 723 F. Supp. at 474.

the nineteen plaintiff states (including Florida and Illinois, the states of residence of two individual plaintiffs), the district court concluded that insurance companies subject to these regulations qualified for the federal antitrust exemption under McCarran-Ferguson.²²¹

The court of appeals found the district court's analysis unconvincing and stated that the pleading of one count (under state law) does not necessarily destroy the foundation of an alternative count (under federal law).²²² In other words, the plaintiffs were not "trapped by [their] pleadings."²²³ The court of appeals also noted that whereas the domestic defendants had pleaded that their business was subject to state regulation, the foreign defendants had argued that they were not subject to any regulation under the doctrine of comity.²²⁴ Thus, by extending McCarran-Ferguson antitrust immunity to the defendants, the district court allowed the defendants, though not the plaintiffs, to rely upon alternative theories.²²⁵ The court of appeals reasoned that since the defendants were not penalized for proceeding under alternative theories, neither should the plaintiffs be penalized, stating "[w]hat is sauce for the goose is sauce for the gander."²²⁶ Therefore, under the Ninth Circuit's reasoning, McCarran-Ferguson does not force plaintiffs to choose either a state or federal remedy at the pleading stage. Rather, McCarran-Ferguson allows plaintiffs to pursue federal antitrust as well as state remedies.²²⁷

3. The "Boycott" Exclusion

Even though a particular activity involves the "business of insurance" and is regulated by state law, it is not immunized from federal antitrust laws if it involves a "boycott, coercion or intimidation."²²⁸

221. *Id.*

222. *Insurance Antitrust Litig.*, 938 F.2d at 928.

223. *Id.*

224. *Id.* at 927-28. For a discussion of the Supreme Court's treatment of the international comity issue in *Hartford Fire Insurance*, see *infra* part III.C.1.

225. *Insurance Antitrust Litig.*, 938 F.2d at 928.

226. *Id.* More fundamentally, the court of appeals reasoned that state insurance laws could not regulate foreign defendants because states do not have the power to regulate beyond their borders. *Id.* Therefore, the Ninth Circuit reasoned, McCarran-Ferguson Act immunity would not attach to foreign defendants. *Id.* As a result, the court of appeals held that the exempt defendant insurers had forfeited their immunity by conspiring with the nonexempt defendant insurers. *Id.* (citing *Royal Drug*, 440 U.S. at 231; *Beltz Travel Serv., Inc. v. International Air Transp. Ass'n*, 620 F.2d 1360, 1366-67 (9th Cir. 1980)). The Supreme Court, however, reversed this holding and the Ninth Circuit's interpretation of *Royal Drug*. See *supra* notes 208-18 and accompanying text.

227. See *Insurance Antitrust Litig.*, 938 F.2d at 928.

228. 15 U.S.C. § 1013(b) (1988).

The greatest difference between the opinions of the district court and the court of appeals in *Insurance Antitrust Litigation* involved the "boycott" issue, which also sparked heated debate among the Supreme Court Justices.

Both the lower courts in *Hartford Fire Insurance* relied upon *St. Paul Fire & Marine Insurance Co. v. Barry*,²²⁹ the seminal and only case prior to *Hartford Fire Insurance* to define the term "boycott" within the context of the McCarran-Ferguson Act. On the basis of relatively fine distinctions and a narrow reading of certain passages in *Barry*, the district court determined that no boycott existed within the meaning of the McCarran-Ferguson Act.²³⁰ After an examination of essentially the same passages, however, the court of appeals arrived at the opposite conclusion.²³¹ The Supreme Court, in contrast, interpreted the term "boycott" to mean something quite different from either of the lower courts' definitions.

The district court in *Hartford Fire Insurance* read the Supreme Court's opinion in *Barry* quite narrowly. Based upon its conclusion that *Barry* required an absolute refusal to deal with policyholders, the district court reasoned that the outcome in *Barry* "turned not on the pressure and compulsion directed at policy holders to submit to curtailed coverage, but on the agreement with competitors not to deal with those policy holders on any terms."²³² In addition to the Supreme Court's *Barry* decision, the district court also relied on a line of cases and commentary which argued that a boycott must involve concerted denials of market access to consumers, rather than mere pressure on other insurers to provide reduced coverage.²³³ The district court eventually concluded:

What the McCarran Act leaves unprotected is conduct which goes beyond the making and implementation of agreements to

229. 438 U.S. 531 (1978). For a discussion of *Barry*, see *supra* notes 54-70 and accompanying text.

230. See *Insurance Antitrust Litig.*, 723 F. Supp. at 475-79.

231. See *Insurance Antitrust Litig.*, 928 F.2d at 928-30.

232. *Insurance Antitrust Litig.*, 723 F. Supp. at 476.

233. *Id.* at 476-78 (citing *Feinstein v. Nettleship Co.*, 714 F.2d 928 (9th Cir. 1983), *cert. denied*, 466 U.S. 972 (1984); *Proctor v. State Farm Mutual Auto. Ins. Co.*, 561 F.2d 262 (D.C. Cir. 1977), *vacated*, 440 U.S. 942 (1979); *Meicler v. Aetna Casualty and Sur. Co.*, 506 F.2d 732 (5th Cir. 1975); *In re Workers' Compensation Ins. Antitrust Litig.*, 867 F.2d 1552 (8th Cir.), *cert. denied*, 492 U.S. 920 and *cert. denied*, 493 U.S. 818 (1989); *UNR Indus., Inc. v. Continental Ins. Co.*, 607 F. Supp. 855 (N.D. Ill. 1984); *Grant v. Erie Ins. Exch.*, 542 F. Supp. 457 (M.D. Pa.), *aff'd mem.*, 716 F.2d 890 (3d Cir. 1982), *cert. denied*, 464 U.S. 938 (1983)). The court also quoted PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 210.2, at 107-08 (Supp. 1988). See *Insurance Antitrust Litig.*, 723 F. Supp. at 477.

do business only on terms acceptable to the participant (even if such agreements would otherwise violate Section 1), such as refusals to deal on any terms and exclusion from alternative sources. Such conduct is not charged here.²³⁴

The court of appeals strongly disagreed with the district court's interpretation and characterization of *Barry* and concluded that the defendants' alleged conduct in *Hartford Fire Insurance* was indeed a boycott within the meaning of the McCarran-Ferguson Act.²³⁵ According to the court of appeals, the district court had placed undue emphasis upon statements in *Barry* which suggested that a boycott involves a total refusal to deal with policyholders.²³⁶ In contrast, the court of appeals relied upon portions of *Barry* which indicated that the mere "enlistment of third parties in an agreement not to trade, as a means of compelling capitulation by the boycotted group, long has been viewed as conduct supporting a finding of unlawful boycott."²³⁷ The court of appeals then noted that defendant Hartford and the other defendant primary insurers had allegedly engaged in such actions by enlisting reinsurers to compel ISO and some of the more reluctant primary insurers to alter their policies.²³⁸ The London reinsurers likewise engaged in such actions, the court noted, by denying retrocessional coverage on policies covering pollution risks.²³⁹

The court of appeals then attempted to articulate a general rule for

234. *Insurance Antitrust Litig.*, 723 F. Supp. at 478 (citations omitted). As the district court explained its reasoning:

The purpose of McCarran Act immunity is to permit joint action by insurers and underwriters within the states' regulatory schemes to formulate policy terms and determine coverage. While it is not a necessary part of the policy development process that the participants would then offer substantially similar policies to the public, it is a consequence that could be reasonably anticipated. To subject the participants in the collective form development process to the risk of antitrust liability for using the product of that process would effectually nullify the McCarran Act. It makes no sense, therefore, for the plaintiffs to rest their boycott claim on the allegation of such an agreement. It is also implicit that joint action comprehends efforts to seek agreement by others, including those who might be unwilling to agree were it not for economic exigencies, and again it makes no sense to assert that such efforts constitute non-immune coercion.

Id. (citations omitted).

235. *Insurance Antitrust Litig.*, 938 F.2d at 930.

236. *Id.* The court of appeals specifically stated that "[t]he district court . . . placed an emphasis that we do not on the [*Barry*] Court's statement that the boycotting insurers there would not deal with the doctors 'on any terms.' The district court supplied italics for this phrase, which is unemphasized in the [*Barry*] Court's opinion." *Id.*

237. *Id.* at 929 (quoting *Barry*, 438 U.S. at 544-45).

238. *Insurance Antitrust Litig.*, 938 F.2d at 929.

239. *Id.*

boycotts under the Act, stating that a boycott occurs where an activity involves “the use of the economic power of a third party to force the boycott victim to agree to the boycott beneficiary’s terms.”²⁴⁰ Under this standard, the court of appeals concluded that the *Hartford Fire Insurance* plaintiffs had alleged sufficient facts to indicate that the defendant insurers had engaged in a boycott, for the defendant reinsurers and London underwriters had allegedly used their economic power—their refusal to reinsure—to compel ISO and the other primary insurers to accept the policy terms that the defendant insurers wanted to sell.²⁴¹

In the most controversial section of the Supreme Court’s *Hartford Fire Insurance* decision, the Court held by a five-to-four vote that the term “boycott” had acquired a very specific and limited meaning under the McCarran-Ferguson Act.²⁴² Justice Scalia, who delivered the opinion of the Court on this issue, began his analysis of the scope of the term “boycott” under the McCarran-Ferguson Act by tracing the origin of the word “boycott” to the story of Captain Boycott and the Irish Land League.²⁴³ Upon examination of the history of Captain Boycott’s misfortunes and several dictionary definitions of the term “boycott,”²⁴⁴ Justice Scalia concluded that there is a clear distinction

240. *Id.* at 930 (citations omitted). In reaching this conclusion, the court of appeals noted that the *Barry* Court had held that the term “boycott” included boycotts directed against both policyholders and competitors alike, and thus the Court’s definition did not exclude from the definition of “boycott” refusals to deal except on the terms demanded. *Id.*

241. *Insurance Antitrust Litig.*, 938 F.2d at 929-30.

242. *Hartford Fire Insurance*, 113 S. Ct. at 2911.

243. *Id.* As Justice Scalia noted, the term “boycott” was first used in the late 19th century “to describe the collective action taken against Captain Charles Boycott, an English agent managing various estates in Ireland.” *Id.* Because Captain Boycott had refused to reduce rents, the entire population of the region collectively resolved not to have any relations with him until he capitulated. *Id.*

244. Justice Scalia examined several dictionary definitions of the term “boycott.” One dictionary defined “boycott” as “[t]o combine in refusing to hold relations of any kind, social or commercial, public or private, with (a neighbour), on account of political or other differences, so as to punish him for the position he has taken up, or coerce him into abandoning it.” *Hartford Fire Insurance*, 113 S. Ct. at 2911 (quoting 2 THE OXFORD ENGLISH DICTIONARY 468 (2d ed. 1989)). Justice Scalia also considered another dictionary definition of the term, defining a “boycott” somewhat differently as “to withhold, wholly or in part, social or business intercourse from, as an expression of disapproval or means of coercion.” *Id.* at 2912 (quoting WEBSTER’S NEW INTERNATIONAL DICTIONARY (2d ed. 1950)).

Black’s Law Dictionary, which was not cited by Justice Scalia, provides a third alternative. It defines a “boycott” as “[a] conspiracy or confederation to prevent the carrying on of business, or to injure the business of any one by preventing potential customers from doing business with him or employing the representatives of said business, by threats, intimidation, coercion, etc.” BLACK’S LAW DICTIONARY 187 (6th

between a true “boycott” and a “concerted agreement to terms.”²⁴⁵ Whereas a boycott involves a refusal to deal on one transaction in order to obtain concessions on another, unrelated transaction,²⁴⁶ Justice Scalia observed, a “concerted agreement to seek terms” involves a refusal to deal on one transaction to obtain concessions *in the same transaction*.²⁴⁷ Justice Scalia noted that leading cases in the fields of antitrust²⁴⁸ and labor law²⁴⁹ also support the distinction between “boycotts” and “concerted agreements seeking terms.”

Although he noted that the term “boycott” only appears in seven nonlabor antitrust cases prior to the enactment of the McCarran-Ferguson Act,²⁵⁰ Justice Scalia only briefly discussed the Court’s *Barry* decision, which is arguably the only prior decision on point. In his only paragraph addressing the case, he asserted that the finding of a boycott in *Barry* was not surprising because “[t]he insisted-upon condition of the boycott . . . bore no relationship . . . to the proposed contracts of insurance that the physicians wished to conclude with St. Paul’s competitors.”²⁵¹ Justice Scalia did not, however, address the rest of the *Barry* decision, including the *Barry* Court’s analysis of the McCarran-Ferguson Act’s legislative history, which appeared to read the term “boycott” quite broadly.

Under Justice Scalia’s definition of the term “boycott,” some of the plaintiff’s allegations in *Hartford Fire Insurance* survived the defendant insurers’ motion to dismiss. Construing the issues of fact in

ed. 1990).

245. *Hartford Fire Insurance*, 113 S. Ct. at 2912.

246. Justice Scalia observed that it is the “expansion of the refusal to deal beyond the targeted transaction,” in which unrelated transactions are used as leverage to achieve desired terms, “that gives great coercive force to a commercial boycott . . .” *Id.*

247. *Id.* In a forceful dissent, Justice Souter claimed that the solicitation of a refusal to deal, even in the primary transaction, constituted a “boycott.” *Id.* at 2905 (Souter, J., dissenting); see *infra* text accompanying notes 255-64 for a more thorough discussion of Justice Souter’s dissent on the boycott issue.

248. *Hartford Fire Insurance*, 113 S. Ct. at 2912-13 (citing *United States v. First Nat’l Pictures, Inc.*, 282 U.S. 44 (1930); *Paramount Famous Lasky Corp. v. United States*, 282 U.S. 30 (1930); *Anderson v. Shipowners’ Ass’n of Pacific Coast*, 272 U.S. 359 (1926); and *Eastern States Retail Lumber Dealers’ Ass’n v. United States*, 234 U.S. 600 (1914)). As Justice Scalia conceded, “concerted agreements seeking terms” are as unlawful as boycotts in the antitrust arena, so no distinction is necessary under the antitrust cases. *Id.* at 2913. Indeed, difficulties in defining “boycott” arise because the term is not used in any antitrust statute other than the McCarran-Ferguson Act.

249. *Id.* at 2913-14 (citing *In re Debs*, 158 U.S. 564 (1895)). Under Justice Scalia’s analysis, a strike seeking better contractual terms in an employment contract does not constitute a boycott; the strike only becomes a boycott if the strikers seek to obtain some advantage from the employer unrelated to the employment contract. *Id.*

250. *Hartford Fire Insurance*, 113 S. Ct. at 2913 n.4.

251. *Id.* at 2914.

a light most favorable to the plaintiffs, the Court held that the complaints sufficiently alleged facts demonstrating that the defendant insurers had engaged in one or more boycotts. For example, as Justice Scalia noted, the complaints alleged that “primary insurers who wrote insurance on disfavored forms would be refused all reinsurance, even as to risks written on *other forms*.”²⁵² Justice Scalia observed that these actions might indeed constitute a boycott “unless the primary insurers’ other business were relevant to the proposed reinsurance contract.”²⁵³ Similarly, the complaints alleged that reinsurers threatened to boycott *all* North American CGL risks, not just CGL policies containing dissatisfactory terms.²⁵⁴

Dissenting on the boycott issue, Justice Souter criticized the majority for employing an “overly narrow” definition of the term “boycott.”²⁵⁵ Although he found common ground with the majority on several points,²⁵⁶ Justice Souter argued that the *South-Eastern Underwriters* Court was the first court to use the terms “boycott,” “coercion,” and “intimidation” in the insurance antitrust context, and noted that the Court had provided a list of prohibited activities.²⁵⁷ Considering this and the *Barry* Court’s guidance, Justice Souter concluded that the term “boycott” does not refer to a “unitary phenomenon.”²⁵⁸ According to Justice Souter, the crucial issue was whether the defendant insurers’ actions constituted “enforcement activities” that would raise the alleged activity to the level of a section 3(b) boycott.²⁵⁹ Justice Souter noted that the defendant primary insurers allegedly “solicited refusals to deal from outside the primary insurance industry as a means of forcing their fellow primary insurers to agree to their terms; the outsiders, acting at the behest of the four, in fact refused to deal with primary insurers until they capitulated.”²⁶⁰

252. *Id.* at 2916.

253. *Id.*

254. *Hartford Fire Insurance*, 113 S. Ct. at 2916.

255. *Id.* at 2903 (Souter, J., dissenting).

256. Justice Souter and the majority agreed on the following points: (1) only refusals to deal involving the coordinated action of multiple actors constitutes a boycott; (2) a boycott need not involve an absolute refusal to deal; (3) a boycott need not involve unequal treatment of the boycott’s targets and its instigators; and (4) concerted activity, while necessary, is not alone a sufficient condition to find a boycott. *Id.* at 2903-04 (Souter, J., dissenting).

257. *Id.* at 2904-05 (Souter, J., dissenting) (citing *United States v. South-Eastern Underwriters Ass’n*, 322 U.S. 533, 535-36 (1944)).

258. *Hartford Fire Insurance*, 113 S. Ct. at 2905 (Souter, J., dissenting) (quoting *Barry*, 438 U.S. at 543 (citation omitted)).

259. *Id.* (Souter, J., dissenting).

260. *Id.* (Souter, J., dissenting).

This pattern of activity, Justice Souter concluded, bore a “striking resemblance” to the activity in *South-Eastern Underwriters* and fell “squarely within even the narrow theory of the § 3(b) exception Justice Stewart advanced in dissent in *Barry*.”²⁶¹

Justice Souter further criticized the majority for ignoring several “crucial features” of the enforcement activities that bound the defendant insurers into a single course of action “recognizable as a § 3(b) boycott.”²⁶² For instance, Justice Souter opined that if the reinsurers had indeed acted “at the behest” of the primary insurers, they could not have been acting entirely in their own independent self-interest.²⁶³ Justice Souter therefore concluded that the plaintiffs’ allegations demonstrated that the primary insurers must have wanted to ensure that no other primary insurers would be able to sell policies that the four defendants did not want to sell.²⁶⁴

Justice Souter and the majority seem to have disagreed on the nature of the relationship between the primary insurers and the reinsurers, a distinction that is important to both opinions. Justice Souter argued that reinsurance constitutes a separate, specialized product, “[t]he availability [of which] affects the ability and willingness of primary insurers to provide insurance to their customers.”²⁶⁵ Consequently, Justice Souter did not view the difference between the primary insurance and reinsurance industries as a mere “technical” distinction.²⁶⁶ The majority, on the other hand, concluded that there was an “integral relationship” between primary insurers and reinsurers and noted that “the terms of the primary coverages are central elements of the reinsurance contract—they are *what* is reinsured.”²⁶⁷

Justice Souter ended his dissent with what may be characterized as a “slippery slope” argument. According to Justice Souter, the majority would conclude that the defendant reinsurers would not be engaged in a boycott if the primary insurers’ other business bore some relation to the proposed policies—for instance, if the reinsurer assumes added

261. *Id.* at 2905-06 (Souter, J., dissenting). As characterized by Justice Souter, Justice Stewart’s dissent advocated limiting the term “boycott” to “‘attempts by members of the insurance business to force other members to follow the industry’s private rules and practices.’” *Id.* at 2906 (Souter, J., dissenting) (quoting *Barry*, 438 U.S. at 565 (Stewart, J., dissenting)).

262. *Hartford Fire Insurance*, 113 S. Ct. at 2907 (Souter, J., dissenting).

263. *Id.* (Souter, J., dissenting).

264. *Id.* (Souter, J., dissenting).

265. *Id.* (Souter, J., dissenting) (quoting Complaint of the State of California, ¶ 34).

266. *Id.* (Souter, J., dissenting).

267. *Hartford Fire Insurance*, 113 S. Ct. at 2907, 2914.

risk where the primary insurer engages in riskier transactions.²⁶⁸ Under the majority's standard, Justice Souter argued, reinsurers that refuse to deal with a primary insurer would not be engaged in a boycott if they could merely show that "(1) insuring the risk in question increases the probability that the primary insurer will become insolvent, and that (2) it costs more to administer the reinsurance contracts of a bankrupt primary insurer (including those unrelated to the risk that caused the primary insurer to declare bankruptcy)."²⁶⁹ Justice Souter concluded by warning that in similar situations decided under the majority's standard, there would be an erosion of "what remains of the § 3(b) exception."²⁷⁰

C. *The Defenses of International Comity and State Action*

In the *Hartford Fire Insurance* litigation, the defendants claimed that two other doctrines should bar the application of the federal antitrust laws. The foreign defendants raised the principle of international comity, and all defendants raised the state action defense.

1. The Principle of International Comity

As a defense against the application of the federal antitrust laws, the foreign reinsurer defendants in *Hartford Fire Insurance* contended that the district court lacked subject matter jurisdiction over the claims brought against them, based on either the Foreign Trade Antitrust Improvements Act of 1982²⁷¹ ("FTAIA") or the doctrine of international comity as articulated in *Timberlane Lumber Co. v. Bank of America, N.T. & S.A.*²⁷²

Under the FTAIA, the Sherman Act does not apply "to conduct involving trade or commerce (other than import trade or import commerce) with foreign nations" unless that conduct "has a direct, substantial, and reasonably foreseeable effect" on commerce within the United States, import trade into the United States, or export trade engaged in by a person within the United States.²⁷³ The *Hartford Fire Insurance* plaintiffs argued that the foreign defendants' conduct

268. *Id.* at 2908 (Souter, J., dissenting).

269. *Id.* (Souter, J., dissenting).

270. *Id.* (Souter, J., dissenting).

271. Pub. L. No. 97-290, 96 Stat. 1246 (1982) (codified at 15 U.S.C. § 6a (1988)). The law added a new section to the Sherman Act.

272. 549 F.2d 597 (9th Cir. 1976). For a thorough discussion of the principles behind the doctrine of international comity and the way in which the courts have applied the doctrine, see *supra* part II.F.2.

273. 15 U.S.C. § 6a (1988).

satisfied the FTAIA's import trade exception, alleging that the London reinsurers had conspired to restrict the terms on which reinsurance policies could be written and to refuse to reinsure "long-tail" risks or risks written on occurrence forms.²⁷⁴ Such coercion and intimidation of primary insurers and individuals who might communicate with regulatory bodies, the plaintiffs alleged, resulted in the unavailability of occurrence liability coverage for many risks.²⁷⁵ The foreign defendants responded that the FTAIA should bar the application of the Sherman Act to their activities because the alleged conduct pertaining to reinsurance transactions involved "wholly foreign commerce."²⁷⁶ The district court, however, concluded that the FTAIA did not preclude Sherman Act jurisdiction because the plaintiffs had "adequately alleged that a decision not to provide reinsurance or retrocessional reinsurance to cover certain types of risks in the United States has a direct effect on the availability of primary insurance in the United States."²⁷⁷ The defendants did not brief the issue on appeal, and the court of appeals affirmed the district court's decision.²⁷⁸

The foreign defendant insurers also raised international comity as a defense to the application of the federal antitrust laws. In *Hartford Fire Insurance*, both the district court and the court of appeals applied several of the *Timberlane* factors, but reached opposite conclusions in almost every instance. The district court held that international comity required abstention from exercising jurisdiction over the foreign defendants,²⁷⁹ but the court of appeals held that international comity did not preclude the exercise of Sherman Act jurisdiction.²⁸⁰ The Supreme Court performed a slightly different analysis of the international comity issue than had the lower courts.²⁸¹ Justice Souter,

274. *Insurance Antitrust Litig.*, 723 F. Supp. at 484.

275. *Id.*

276. *Id.* at 486. The district court noted that a large portion of the of transactions involved in the purchase of reinsurance occur in London. *Id.* at 485. The court also noted, however, that the sequence of transactions actually commences in the United States when a consumer purchases insurance from a primary insurer who then decides to purchase reinsurance from the reinsurers in London. *Id.* More importantly, the court observed that the alleged refusal to sell reinsurance to certain U.S. primary insurers would produce substantial effects in the U.S., thereby precluding any characterization of the alleged activity as "wholly foreign commerce." *Insurance Antitrust Litig.*, 723 F. Supp. at 486.

277. *Id.* (citation omitted).

278. See *Insurance Antitrust Litig.*, 938 F.2d at 932.

279. See *Insurance Antitrust Litig.*, 723 F. Supp. at 487-90.

280. See *Insurance Antitrust Litig.*, 938 F.2d at 932-34.

281. The lower courts first determined whether FTAIA granted the district court Sherman Act jurisdiction and then examined whether international comity precluded exercising that jurisdiction. The extent to which the Supreme Court analyzed the juris-

writing for the five-to-four majority, first commented that the Sherman Act does indeed apply to “foreign conduct that was meant to produce and did in fact produce some substantial effect in the United States.”²⁸² Justice Souter then asserted that the determining factor and only “substantial question” in the *Hartford Fire Insurance* case was whether American law truly conflicted with the relevant British law.²⁸³ In arguing that American and British law did in fact conflict, the foreign reinsurers claimed that Parliament had established a comprehensive regulatory scheme for the London reinsurance market and that the London reinsurers’ conduct was consistent with that scheme.²⁸⁴ Justice Souter responded, however, that the existence of such a regulatory scheme in Great Britain did not demonstrate a conflict, and that the London reinsurers’ compliance with the British regulations merely indicated that the conduct was lawful in Great Britain.²⁸⁵ Thus, the Court concluded that “[s]ince the London reinsurers do not argue that British law requires them to act in some fashion prohibited by the law of the United States, or claim that their compliance with the laws of both countries is otherwise impossible, we see no conflict with British law.”²⁸⁶

In his dissent, Justice Scalia argued that it was “unimaginable” that the assertion of legislative jurisdiction would be considered reasonable, and found it “inappropriate to assume” that Congress intended American courts to exercise extraterritorial jurisdiction in these circumstances.²⁸⁷ Claiming his argument was substantive, not jurisdictional, Justice Scalia proceeded from the premise that even if

dictional issue under FTAIA or notions of international comity is not entirely clear. The Court specifically found that Congress, in enacting FTAIA in 1982, failed to state “whether a court with Sherman Act jurisdiction should ever decline jurisdiction on the grounds of international comity.” *Hartford Fire Insurance*, 113 S. Ct. at 2910. The Court noted that even assuming that a court may decline to exercise Sherman Act jurisdiction, international comity would not have precluded the exercise of such jurisdiction in this case. *Id.* Such a statement arguably implies that an international comity analysis was not required. The Court, however, subsequently considered whether a conflict existed between the relevant domestic and foreign law, a consideration of international comity in itself. *Id.*; see also *Mannington Mills, Inc. v. Congoleum Corp.*, 595 F.2d 1287, 1297-98 (3d Cir. 1979) (considering the conflict between foreign and domestic law in examining international comity).

282. *Hartford Fire Insurance*, 113 S. Ct. at 2909 (citations omitted).

283. *Id.* at 2910.

284. *Id.* The British Government, appearing as amicus curiae in the *Hartford Fire Insurance* case, agreed that application of the FTAIA would conflict with the British law. *Id.*

285. *Id.*

286. *Id.* at 2911.

287. *Hartford Fire Insurance*, 113 S. Ct. at 2921 (Scalia, J., dissenting).

jurisdiction exists, a nation should refrain from exercising jurisdiction if that exercise is "unreasonable."²⁸⁸ Justice Scalia observed that the British government had established a comprehensive scheme regulating the London reinsurance market and that it had a strong interest in doing so.²⁸⁹ Moreover, Justice Scalia reasoned, because the McCarran-Ferguson Act permits state law to displace the Sherman Act except where the activity constitutes a "boycott," federal regulation of the reinsurers was of only "slight" importance to the United States.²⁹⁰ Accordingly, Justice Scalia concluded that "[r]arely would these factors point more clearly against application of United States law."²⁹¹

2. The "State Action" Defense

Although the defendants contended that the state action doctrine precluded the application of the federal antitrust laws to their activities, neither the district court nor the court of appeals in the *Hartford Fire Insurance* case had the benefit of the Supreme Court's guidance in *FTC v. Ticor Title Insurance Co.*²⁹² In response to the defendants' state action argument, the plaintiffs contended that while the states may have authorized voluntary joint action, they did not authorize coercion or boycotts by private insurance companies.²⁹³ The district court, however, concluded that immunity under the state action doctrine could also arise from a state's "authority to conduct collective policy development activities."²⁹⁴ Applying the two-prong inquiry set forth in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum*,

288. *Id.* (Scalia, J., dissenting). Justice Scalia relied upon 1 RESTATEMENT (THIRD) THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 403(1) (1987) for this "reasonableness" standard. See *Hartford Fire Insurance*, 113 S. Ct. at 2921 (Scalia, J., dissenting). Justice Scalia cited several factors to be considered in determining what constitutes a reasonable exercise of jurisdiction: "the extent to which the activity takes place within the territory [of the regulating state]; the connections, such as nationality, residence, or economic activity, between the regulating state and the person principally responsible for the activity to be regulated; the character of the activity to be regulated, the importance of regulation to the regulating state, the extent to which other states regulate such activities, and the degree to which the desirability of such regulation is generally accepted; the extent to which another state may have an interest in regulating the activity;" and "the likelihood of conflict with regulation by another state." See *id.* (Scalia, J., dissenting) (quoting 1 RESTATEMENT (THIRD) THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 403(2)(a)-(h) (1987)).

289. *Hartford Fire Insurance*, 113 S. Ct. at 2921 (Scalia, J., dissenting).

290. *Id.* (Scalia, J., dissenting).

291. *Id.* (Scalia, J., dissenting).

292. 112 S. Ct. 2169 (1992). For a discussion of the state action doctrine as interpreted by the Supreme Court in *Ticor* and its effect on the application of the antitrust laws to the insurance industry, see *supra* part II.F.1.

293. *Insurance Antitrust Litig.*, 723 F. Supp. at 480.

294. *Id.*

Inc.,²⁹⁵ the district court determined that each state had articulated express policies permitting joint rate filings, thereby fulfilling the first requirement of *Midcal*, and that the existence of state supervision in the form of “approval, disapproval, or modification of the end product of the collective action” satisfied *Midcal*’s second requirement.²⁹⁶

The Ninth Circuit disagreed with the district court’s conclusion, stating that “nothing in the affidavit evidence submitted by the defendants shows that the relevant states supervised or approved the boycotts used to produce agreement on the forms.”²⁹⁷ The court of appeals distinguished the alleged anticompetitive activities from what the states had actually regulated:

[S]tate approval of one activity is not state approval of a related but distinct activity. The alleged anti-competitive conduct in the present case . . . was neither a reasonable nor necessary consequence of the conduct regulated and approved by the state. The agreements to refuse to reinsure were not state action.²⁹⁸

Thus, the court of appeals held that the state action doctrine did not immunize the defendant insurers from antitrust liability.²⁹⁹ The Supreme Court did not address the state action doctrine, and thus the opportunity for further clarification of the doctrine in the context of insurance antitrust regulation was lost.

IV. REGULATION OF THE INSURANCE INDUSTRY IN THE AFTERMATH OF *HARTFORD FIRE INSURANCE*: A PLEA FOR RATIONAL DISCOURSE

For several reasons, the Supreme Court’s *Hartford Fire Insurance* decision is certain to bring the issue of insurance regulation to a rolling boil once again. First, the *Hartford Fire Insurance* opinion seems to provide the first diminution of federal power over insurance since 1969. This diminution and limitation is small, of course, reflected only in a reduction in scope of the term “boycott.” Nevertheless, this reduction is the first such action by the Supreme Court in over thirty years. Perhaps more important than this slight change in the law is the convoluted and confused nature of the decision itself. The operative “boycott” portion of the decision consists only of a fragile five-to-four majority. The Court’s view on this matter is unlikely to change in the

295. 445 U.S. 97 (1980). For a discussion of *Midcal*, see *supra* notes 118-27 and accompanying text.

296. *Insurance Antitrust Litig.*, 723 F. Supp. at 480-81.

297. *Insurance Antitrust Litig.*, 938 F.2d at 931.

298. *Id.* (citations omitted).

299. *Id.*

near future, barring any unexpected changes in the makeup or position of the Court. It is also important to note that the Court did not rely on any broader "states' rights" argument, nor on grounds of policy that regulation of the insurance industry is better left to the states. The Court's reliance on a narrow definition to resolve a case with such massive policy implications reveals an unwillingness or an inability to ascertain overriding policy objectives from the Act and its legislative history.

Moreover, the Court's decision places many of the current problems of insurance regulation on full display. The international law problems in the *Hartford Fire Insurance* litigation only exacerbate the already difficult question of regulation. It is extremely difficult for the federal government to regulate the international aspects of the insurance industry under the antitrust laws. It is virtually impossible for the states to do so. The split in the Supreme Court underlines the difficulties inherent in regulating interstate firms at any level. Furthermore, the case demonstrates that the state action doctrine is yet another complicating factor in the regulation of the insurance industry. This doctrine, modified through the *Ticor* case, provides another limitation on the use of the antitrust laws to regulate the insurance industry. Indeed, under the state action doctrine, states may be able to displace the effectiveness of the antitrust laws in regulating insurance, even in the absence of the McCarran-Ferguson Act.

The Court's opinion, although demonstrating many of the problems inherent in the current scheme of insurance regulation, at least provides some solutions to improving the current scheme. The "activities" standard of *Hartford Fire Insurance*, which looks to the particular activity in which the insurance company engages rather than to the entity itself to determine whether the McCarran-Ferguson antitrust exemption applies, presents a fairly flexible and realistic standard that can be adjusted to the realities of the insurance world. The adoption of a broad standard that would exempt insurance companies from federal antitrust regulation in all circumstances would be somewhat dangerous and might also provide an incentive to businesses to inoculate themselves from federal authority by engaging in various insurance activities. As the insurance industry develops, new risks are created, and insurance companies are frequently integrated into other financial organizations. It is therefore important to have a rule that permits the courts to apply the original and essential purposes of the Act. The "activity rule" does just that.

The Court's division and the finely worded nature of both parts of the opinion indicate something much larger about the state of insurance

regulation. The insurance industry is *sui generis*, and many of the traditional rules of antitrust law and business regulation in general simply cannot apply. It is virtually impossible to argue that *any* single form of regulation of insurance would be effective for the entire industry. The Court's difficulty is reflective of the larger question: How should insurance be regulated? The Court cannot agree, and neither can anyone else. A review of the background of the McCarran-Ferguson Act and its judicial history leads almost inevitably to the conclusion that the Act is not doing an effective job of dividing regulation of the insurance industry between the states and the federal government. Virtually no one is satisfied with the current state of affairs.

In the almost half-century since the McCarran-Ferguson Act was passed, a number of changes have occurred that call the purposes of the Act into question. Insurance has become big business, far larger than it was in 1945, with larger firms operating on a national and international scale. Insurance has become far more integrated with other financial services, including investment firms and banking, and therefore has greater influence upon the rest of the economy than it did in 1945. International firms, including firms from old enemies and devastated allies of World War II, play a much larger role than they did fifty years ago. Underwriting and actuarial techniques, enhanced by computer technology, are far more sophisticated than in the "green eye shade" days of the mid-1940s. Moreover, the judicial and administrative treatment of the antitrust laws has changed dramatically since the end of World War II.

In this current climate, there appears to be no good reason to provide a blanket exemption from the antitrust laws for virtually all activities of the insurance industry. The purposes of the exemption were initially three-fold: (1) to protect property and liability carriers from antitrust exposure for a number of information and rate-sharing activities; (2) to protect existing state legislative schemes; and (3) to forestall federal regulation under the activist Roosevelt administration.³⁰⁰ The protection of existing state legislative schemes is not, by itself, a satisfactory reason for the continuation of McCarran-Ferguson. Similarly, mere fear of federal power should not be a basis for policy. This sort of jealous self-protection and automatic response is the stuff of ideology, not policy. Federal regulation is not inherently bad, nor is state regulation inherently good. A regulatory scheme should instead be judged dispassionately and objectively with an eye to

300. Weller, *supra* note 28, at 590-91; *see supra* text accompanying note 30.

the regulatory goals.

Certainly, the need to share information in the property and liability insurance areas may require an exemption for that particular activity; the burden to show the need for an exemption of other activities, however, should be on those requesting the exemption. For example, the antitrust exemption should not be extended to inter-industry restraints of trade.³⁰¹ Moreover, if the need for rating organizations indeed compels exempting the "business of insurance" from federal antitrust laws, a major question remains: Why does the exemption apply to the entire insurance industry when it appears that only property, casualty, and liability insurers need the broad-based statistical data and cooperative actions? Apparently, life, health, and specialty³⁰² insurers could survive without the exemption. This query demonstrates the McCarran-Ferguson Act's attempt to utilize one regulatory scheme for all of the multifarious insurers and the obvious lack of "fit" that results.

Among the difficulties inherent in the regulatory environment encountered by today's insurance company is a complex state-by-state regulatory scheme. National and international firms find that they must comply with fifty different regulatory schemes. The different approaches of the fifty states to regulation has resulted in a belief that two very different kinds of regulatory extremism have taken place. On one hand, it might be argued that the regulatory apparatus of some states has been "captured" by the insurance industry, which then ignores the needs of other constituencies, including consumers. On the other hand, opponents fear that some other states' insurance commissions have been "captured" by the other side—the consumer advocates—who engage in "industrial lynching" of the insurance community.

301. Cf. Weller, *supra* note 28, at 621-40. Weller argues that the McCarran-Ferguson Act should not exempt (1) actions of insurance companies that adversely affect competition in another industry; or (2) providers of insured goods or services that restrain trade in their own markets through the use of insurance. *Id.* at 622-24. An example of the former would be agreements between insurance companies and specific vendors or providers (*e.g.*, auto glass repair shops, pharmaceutical companies, or health care providers) to provide services to insured parties at specific rates. *See id.* at 622. An example of the latter would be the establishment of captive insurance companies by providers of a particular good or service (*e.g.*, the establishment of a prescription insurance program by pharmaceutical firms). *See id.* at 623. While these agreements do not necessarily involve antitrust violations, no logical reason exists to exempt possible antitrust violations simply because they may carry the broad label "insurance."

302. For example, one small company writes only "hole-in-one" insurance for golf outings. There seems to be no logical reason for this company to be exempt from the antitrust laws.

There are, of course, many good examples of balanced regulatory schemes, and true examples of capture by either the industry or consumer advocates are probably quite rare and exaggerated by the antagonists on both sides. In all likelihood, most states' regulatory schemes are operated in a manner that reflects state values and opinions. It has been conversely argued, of course, that federal regulation is not the answer, and will result in an overlay to state regulation, creating "a dual, duplicative, and potentially inconsistent system of regulation."³⁰³

State law is also simply unable to deal with international insurers in any effective manner. Huge international firms, including both direct writers, reinsurers, and retrocessional insurers are simply too large, too complex, and too powerful for most states to control. Even the federal government may not be able to deal with such firms. The most important holding of *Hartford Fire Insurance* may indeed be Justice Souter's opinion that international insurance firms are subject to the federal antitrust laws if there is conduct that is intended to, and which in fact does, produce some substantial effect in the United States.³⁰⁴ The case was somewhat close, however, and only one vote stood between Justice Souter's view and Justice Scalia's complete surrender of federal antitrust scrutiny of foreign insurers in all cases in which foreign law conflicts with American law.

The McCarran-Ferguson Act was designed for a simpler time, one that is gone forever. While federal regulation may not be the answer, it should not be rejected in all instances. For example, the weight and power of the federal government may be necessary to provide a level playing field for domestic and international firms and to prevent foreign firms from bullying domestic insurers through reinsurance or retrocessional insurance transactions. Similarly, the federal role over areas that demand uniformity, such as insurer solvency, must be expanded. On the other hand, state law should retain its traditional role for many aspects of insurance, including regulation of brokers and sales agents, small local firms, and local underwriting problems. In other areas, it may be possible to adopt state compacts or uniform laws that provide uniformity between states while retaining state hegemony over an area. If Congress chooses to exercise federal regulatory power through the continued application of the McCarran-Ferguson Act, however, it should carefully consider some of the judicially created rules that now apply to the Act. For example, the activity rule

303. Melendez, *supra* note 28, at 304.

304. See *supra* text accompanying note 282.

applied in *Hartford Fire Insurance* should be retained and perhaps even strengthened by statutory adoption.

A third alternative may also be useful for some forms of insurance regulation. Uniform state laws, adopted through a variety of techniques, may provide the necessary uniformity *and* flexibility. Such laws may be adopted through interstate cooperation, in a manner akin to the adoption of the Uniform Commercial Code,³⁰⁵ through some interstate compact,³⁰⁶ or as a result of federal mandates.

The incredibly variegated world of insurance cannot be effectively regulated in any single way. None of the three forms—federal, state, or state-cooperative—will work for all areas. It is time to critically examine McCarran-Ferguson once again for the benefit of both the insurers and the insured. Such a re-examination must also reject knee-jerk responses. A creative, flexible, and rational system of regulation can be devised, sharing power between the federal government where necessary and the states where possible. The *Hartford Fire Insurance* case may provide the catalyst for reasoned and constructive change, that will put to rest fifty years of inefficiency and irrationality.

Insurance and financial services are certain to remain among the largest and most lucrative of the global service industries for many decades to come. It is time to create a system of regulation that adequately protects consumers and which allows for industry growth, development, and freedom of action. It is time to put aside an antiquated law that has no relation to realities of the marketplace.

305. See L. H. Otis, *Congressman Backs State Compact Plan*, NATIONAL UNDERWRITER (PROPERTY & CASUALTY/RISK BENEFITS MANAGEMENT EDITION), Aug. 23, 1993, at 3.

306. See Cynthia Crosson, *NAIC Model Laws Pass in New Jersey*, NATIONAL UNDERWRITER (PROPERTY & CASUALTY/RISK BENEFITS MANAGEMENT EDITION), Aug. 16, 1993, at 3. This twelve-bill package permits accreditation by the National Association of Insurance Commissioners, and includes bills covering financial solvency oversight, reinsurance regulation, life risked-based capital and other areas. *Id.* at 31. The law failed in New York, presumably because "the legislators would not tolerate having unelected state regulators tell them what laws they have to pass." *Id.*