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Active State Role in the Regulation of Title Search Fees Required to Shield Insurance Companies from Liability

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Recent Cases

Active State Role in the Regulation of Title Search Fees Required to Shield Insurance Companies From Liability

In *Federal Trade Commission v. Ticor Tile Insurance Co.*, 112 S.Ct. 2169 (1992), the United States Supreme Court held that title insurance companies are not protected from antitrust prosecution when title search fees are fixed by state regulation and the state does not take a substantial role in the active supervision of the fees. Furthermore, the Court found that negligible levels of state regulatory supervision did not immunize the title insurance companies.

Alleged Horizontal Price Fixing

Title insurance policies insure against any unknown defects in the title or ownership of real estate. Many states throughout the country had authorized private rating bureaus to establish uniform rates for title insurance premiums, search fees, and examination charges. The appropriate state agencies then either approved or rejected the recommended fees.

The Federal Trade Commission ("FTC") filed a complaint against six of the nation's largest title companies, alleging horizontal price fixing. The five companies (the sixth settled in a consent agreement with the FTC) comprised about 60 percent of the $1.35 billion title insurance industry. The FTC did not challenge the practice of setting uniform rates for the insurance premiums, but rather objected to the rate setting for the title search, examination, and settlement fees. The complaint alleged a violation of § 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. § 45(a)(1), which forbids "[u]nfair methods of competition in or affecting commerce."

In 1985, the FTC initially complained of this rate-setting practice in thirteen states, yet declined to pursue the matter in five of these states. Later, upon the recommendation of the Administrative Law Judge ("ALJ"), the FTC dropped the complaint against two of the remaining states, thus, leaving only six states subject to the action.

However, after the FTC filed its complaints, the title insurance companies abandoned this rate-setting system because many private treble damage suits were filed against them. Nonetheless, the ALJ held that the complaint was still valid because nothing prevented the companies from resuming the rate setting practice. Therefore, the ALJ conducted a hearing to examine the alleged antitrust violations and to consider the companies' state-action immunity defense.

The State-Action Immunity Doctrine

If a state authorizes and supervises anti-competitive conduct, participants in that conduct may enjoy immunity from liability arising from that conduct under the state-action immunity doctrine. The doctrine of state-action immunity preserves the authority of the states to establish beneficial price fixing regulatory schemes that might otherwise violate federal antitrust laws. The United States Supreme Court established a two part test in *California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc.*, 445 U.S. 97, 100 S. Ct. 937, 63 L. Ed. 2d 233 (1980), to determine when state activity deserves immunity. The first part of the *Midcal* test requires the state to formulate an express policy acknowledging the anticompetitive scheme. The second part of the *Midcal* test requires the state's active supervision of the private actors participating in the regulatory program. Where both parts of the test are satisfied, the state-action immunity doctrine bars antitrust claims.

The Midcal *Test and Lower Court Decisions*

In the administrative hearing, the ALJ found antitrust violations in only two states, Connecticut and Wisconsin, because they failed to satisfy the *Midcal* test. But on appeal to the FTC Review Commission, the Commission found antitrust violations by the title insurance companies in all six states. In reaching this decision, the Commission determined that the title companies were not entitled to state-action immunity because: (1) the level of state supervision of the rate setting practice was insufficient to satisfy the second prong of the *Midcal* test in four of the states; and (2) the other two states' statutes did not contain a policy sufficient to satisfy the first prong of the *Midcal* test.

On appeal, the United States Court of Appeals for the Third Circuit reversed the decision because it found that state supervision of the rating bureaus was sufficient to grant immunity. The Third Circuit applied the standard that a state's supervision is sufficient when state law authorizes and operates a regulatory program.

The United States Supreme Court granted review of the Third Circuit decision. However, since the FTC relinquished its claims against the two states, the Court only considered the four states that failed the second prong of the *Midcal.*

State's Supervision Insufficient

The Supreme Court reversed the decision of the Third Circuit because it found that the supervision in two states did not rise to a level sufficient to warrant immunity from the antitrust laws. However, the Court could not determine the adequacy of the supervision in the remaining two states and therefore remanded the decision to the Third Circuit to re-examine this issue.

The Supreme Court's decision focused on the second prong of the *Midcal* test. The Court criticized the Third Circuit for adopting a standard that amounted to a mere potential for supervision rather than a stricter standard of active supervision. The Court held that a state must play a substantial role in determining the specifics of the state policy and not merely rubber stamp an agreement among the private parties. Moreover, because a negative option regulatory program setting the prices and the rates the private companies proposed became effective unless expressly vetoed by the state, the Court placed the burden of proof on the companies to show that the states adequately supervised the rate-setting process.

In light of this strict standard, the Court examined the programs established in the two states that lacked adequate supervision. Based on the factual findings of the ALJ, the Court noted that in both states, the rate-setting programs lacked any supervision whatsoever. Thus, the Court found that the level of supervision for these two states could not support a grant of immunity.

Additionally, the Supreme Court offered grounds to distinguish this ruling in future applications. First, the Court noted that the gravity of the offense here was extreme: horizontal price fixing is the most "pernicious" antitrust offense. Second, the Court pointed to the dominating role of the private companies in the rate setting process. Third, the Court cited the clear lack of state supervision, not merely a temporary lapse.

Dissent Fears Increased Litigation

The three dissenting justices noted that the controversy concerning the application of the state-action immunity doctrine is far from finished. They regarded the strict standard adopted by the majority as ambiguous, untenable, and as litigation-breeding. Also, the dissenters stated that previous applications of the *Midcal* test examined whether a state had the power to reject or control the proposed uniform rates. The dissent also stated that the strict active supervision standard adopted by the Court required close scrutiny into whether the states played a substantial role in the rate setting process. However, since the Court neither defined this standard nor established any benchmarks, the dissent reasoned that its application would be arbitrary at best.

Furthermore, the dissent reasoned that companies would now be less likely to participate in negative option regulatory programs because the burden is on them, under penalty of antitrust treble damages, to prove that the states substantially performed their duties. ❖

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FTC Not Required to Rely on Extrinsic Evidence to Determine Fraudulent Implied Claims in Advertising

In *Kraft, Inc. v. Federal Trade Commission*, 970 F.2d 311 (7th Cir. 1992), the Seventh Circuit Court of Appeals held that a manufacturer violated the Federal Trade Commission Act when it misrepresented the content of its cheese slices. Furthermore, the court stated that its own reasoned analysis, rather than extrinsic evidence, may be used in determining the implied claims contained in the challenged advertisements.

Kraft Singles Advertisements Fraudulent

In the early 1980's, Kraft, Inc. ("Kraft") began losing market share in the sliced cheese market. The loss of market share resulted from the introduction of imitation cheese slices, which were advertised as less expensive but equally nutritious as Kraft's Singles, a processed cheese slice. Kraft responded with an advertising campaign to inform consumers that Singles cost more because they are made from five ounces of milk rather than cheaper ingredients. The advertisements also focused on the calcium content of Singles.

Although Kraft used five ounces of milk to make each Single, roughly 30 percent of the calcium was lost in processing. Additionally, the vast majority of imitation slices sold in the United States contained about 15 percent of the U.S. daily recommended allowance of calcium per ounce, approximately the same amount as in Singles.

The Federal Trade Commission ("FTC") complaint alleged that Kraft's advertisements made two implied claims that violated the Federal Trade Commission Act ("the ACt"), which makes it unlawful "to engage in unfair or deceptive commercial practices or to induce consumers to purchase certain products through advertising that is misleading in a material respect." The FTC complaint charged that Kraft's advertising campaign violated the Act by materially misrepresenting the calcium content and relative calcium benefit of Singles by implying that a Single contains the same amount of calcium as five ounces of milk ("Milk Equivalency Claim") and that Singles contain more calcium than imitation slices ("Imitation Superiority Claim").

One of the two advertisements at issue in this case featured a young girl eating a Single as a narrator said ". . . Imitation slices use hardly any milk. But Kraft has five ounces per slice. Five ounces. So her little bones get calcium they need to grow . . ." Later, in the same ad, milk was poured into a glass until it reached a mark denoted five ounces. In January 1986, Kraft revised the script of the advertisements from "Kraft has five ounces per slice" to "Kraft is made from five ounces per slice." In March 1987, Kraft added the disclosure "one 3/4 ounce slice has 70 percent of the calcium of five ounces of milk" as a subscript on the television ad and as a footnote in the print ad.

The second ad in controversy, em-