Antitrust Comes Calling On The Insurance Industry

JAMES MORSCH

The insurance industry has enjoyed six decades of nearly total exemption from the country's antitrust laws thanks to the McCarran-Ferguson Act. A growing chorus of antitrust enforcers and legislators, concerned about the ability of state insurance departments to regulate unfair and anticompetitive insurance practices and to protect against large scale insurance-related failures, are calling for increased federal oversight of the insurance industry and passage of legislation aimed at abrogating, in whole or part, the McCarran-Ferguson Act. Insurers face an uncertain regulatory future where practices that have become commonplace over the past half century may be subject to increased antitrust scrutiny and challenge by the federal government and private litigants.

Passed in 1945, the McCarran-Ferguson Act largely removed the insurance industry from the two primary federal antitrust statutes, the Sherman and Clayton Acts, on the assumption that state law would adequately regulate the "business of insurance." The only exception to this rule was federal law was to govern efforts by or agreements between insurers to "boycott, coerce or intimidate." For all practical purposes, since state law regulates insurance rates and forms (i.e., the prices charged and policy terms utilized by insurers), the McCarran-Ferguson Act exempts most of the types of conduct that give rise to traditional antitrust claims in other industries. The federal government has occasionally challenged the merger of two large carriers or methods of unfair competition used by insurers and their agents or brokers, but these cases have been the exception to the general rule that antitrust regulators are to stay out of the business of insurance.

As a result, at least until recently, insurers have been relatively free to exchange sensitive premium and loss data and to jointly push for the adoption of insurance products, terms and conditions by state regulators and their proxies without much, if any risk, of investigation, review or challenge by the Antitrust Division of the Department of Justice or the Federal Trade Commission. Critics of the McCarran-Ferguson Act claim that this has led to an inordinate amount of industry consolidation, higher prices and a variety of business practices detrimental to consumers. Supporters of the exemption say that the McCarran-Ferguson Act has spurred industry-wide innovations, leveled the playing field between large and small carriers, and fostered transparency in the premiums charged and losses covered by the industry.

The rise in the cost of insurance, complaints about insurers moving out of states battered by natural disasters, the adoption of insurance products that are poorly understood by consumers, and the recent spate of financial institution failures including the federal bailout of one of the country's largest insurers have called into question whether leaving regulation of the business of insurance to state insurance commissioners is a good idea. Many observers believe that state insurance departments have been effectively co-opted by insurers, lack the authority and tools to keep up with changes in the industry, and do a poor job evaluating and controlling the systemic risks inherent in the scale, insurance institutions. Others question the self-regulating nature of some aspects of the industry, pointing out that there is a fair amount of evidence that markets on the fringe of the insurance industry like credit-default swaps do not adequately self-regulate when left to their own devices.

Earlier this year, a bill entitled the Insurance Industry Competition Act of 2009 was introduced in the House of Representatives. The bill, which at the date of this writing is still in committee, would permit federal scrutiny of insurance practices and expressly authorize the Antitrust Division and Federal Trade Commission to issue guidance to the industry on their enforcement policies regarding "joint activities in the business of insurance." Similar bills have failed to obtain Congressional approval in the past and opposi-

tion to the bill's passage likely will be stiff. Nonetheless, with a new Administration in Washington committed to more vigorous antitrust enforcement and an ongoing effort to federalize portions of the insurance business, the Insurance Industry Competition Act could gain substantial traction or aspects of it could be folded into heath care reform legislation being pushed through Congress.

Even if legislation intended to abrogate the McCarran-Ferguson Act does not pass Congress, there are growing signs that federal antitrust regulators are going to more closely scrutinize industries that traditionally have enjoyed immunities from the antitrust laws like the insurance industry. Recently, the Department of Justice launched a wide-scale investigation of practices in the agricultural industry which, like the insurance industry, is supposed to be highly regulated. This investigation and comments by Obama Administration officials evidence a desire to pull the curtain back on industries traditionally exempted from the antitrust laws.

Greater competitive oversight of the insurance industry is sure to follow this trend. Already, consumer protection advocates are pushing Congress to regulate mortgage, title and health insurance on the grounds that the payment of commissions in connection with these products is done behind the backs of consumers and results in higher prices and limited competitive choices. Others challenge what they see as the nearly cartel-like control many groups of insurers have over information relating to the cost and availability of competitive insurance products. Still others point to studies showing increased price competition in states where insurers must obtain advance approval of changes in insurance rates as evidence that the federal government should more actively intervene in certain insurance markets.

Where does all of this leave insurance industry participants? Unfortunately, in a state of flux. Nonetheless, there are a number of things, beyond lobbying Congress and the Administration, that the insurance industry can do now to prepare for the day when the antitrust regulators come calling. First, insurers should be enhancing their antitrust compliance programs and taking steps to educate their business people on the nuances of antitrust law. Second, insurers should consider conducting a top-down review of their joint activities with their competitors to see if the company is engaging in communications or activities that might be construed as an act of "boycott, coercion or intimidation" by antitrust regulators. Third, because there are antitrust immunities and defenses available beyond the McCarran-Ferguson Act, insurers should be brushing up on such things as the filed rates doctrine, the meeting-the-competition defense, the rule of reason for joint venture activities, and the state action doctrine. Having had the benefit of more than sixty years of virtual exemption from antitrust scrutiny, insurers might be slow to adapt to what promises to be a new and challenging era for the industry, but those companies that invest in preparing for the future are the ones most likely to come out ahead in it.

James Morsch is a partner with Butler Rubin Saltarelli & Boyd LLP, a Chicago litigation boutique. He concentrates his practice in complex commercial litigation, including counseling companies and litigating antitrust and other competition law matters. The views expressed are personal to the author.