Comments To The Antitrust Modernization Commission On

Statutory Immunities and Exemptions from Antitrust Law

Submitted by

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Summary: These comments focus on the statutory exemptions issues raised by the AMC. Exemptions should be limited and their proponents should have the burden of establishing the need for an exemption. While procedural reforms and *ex ante* cost benefit analysis would be helpful, it is questionable how much impact these changes would have. A standard for strict construction of any exemption can reduce adverse effects. Such a standard can be implemented either as a matter of judicial action or legislative command. Because of the inherent dynamics of markets, exemptions ought to have limited duration. Sunset provisions are one option but giving agencies oversight over exemptions with the authority to terminate them may be a better option in some circumstances. The specific statutes the AMC has targeted include two, export cartels and fishing cooperatives, where the statutes are not used or relevant. They should be repealed. The agricultural exemptions involve both protections of farmer cooperatives and government authorized cartels in some commodities. The more serious competitive issues arise in the later category and particularly in the context of dairy products. The suggestion is that the AMAA should be modified to reduce or eliminate its anticompetitive impact. Similarly, the Shipping Act is no longer necessary given the fundamental changes in the industry and the rationales for protecting the insurance industry as a whole from antitrust lack merit although there may be a case for a safe harbor for some limited protection for joint pooling and analysis of loss data in property and casualty insurance.

Introduction

I have been a teacher and scholar of antitrust and competition law for more than three decades. A substantial part of my scholarly life has been directed to studying the interaction between antitrust law and other regulatory regimes that often provide full or partial exemption from antitrust law. I have recently been engaged in focused studies of several statutory exemptions including those affecting agricultural markets. Because my recent work has focused on statutory exemptions and modifications of antitrust law, I will limit these comments to Part A of the questions that the AMC has posed. I have divided my comments into two sections. The first part responds to the AMC's general questions concerning exemptions and immunities. The second part addresses briefly the specific exemptions that the commission has indicated it contemplates reviewing in more detail.

1. When and How Should Congress Provide Statutory Exemptions from Antitrust?

In general Congress should be skeptical of any request for statutory exemptions from antitrust law. It has not developed the capacity to engage in the kind of fine grained analysis of complex legal and factual questions necessary to resolve the merits of such requests. It is ironic, at least, that Congress requires administrative agencies to conduct detailed analysis of the problem to be remedied, the available alternatives, and the likely costs and benefits of choosing each alternative before adopting regulations. Yet Congress, itself, grants exemptions from antitrust that legalize otherwise unlawful exploitative and exclusionary conduct without any comparable review of the projected costs or benefits of such statutes. It would be heartening if Congress were to adopt procedures that would generate a thoughtful review of the purported problem, an analysis of options and some estimate of the expected gains and losses to the economy that would result from the adoption of different options. The AMC should certainly reommend such a procedural reform even if Congress is unlikely to adopted it.

In addition, given the basic national commitment to the competitive market as the primary method for organizing our economy, the proponents of an exemption should bear the burden of convincing Congress that an exemption is warranted. That said, absent some change in the procedures of the legislative process, it is hard to see how such a burden can be operationalized except in a precatory way. The courts are pretty clear that Congress can find the facts as it sees fit. This is sometimes unfortunate, but it is probably a necessary element of separating the branches of government. See, *Board of Trade of City of Chicago v. Olsen*, 262 US 1 (1923)(upholding the validity of the Grain futures Act, 42 Stat. 998 (1921) despite serious questions concerning the accuracy of the factual record on which Congress relied).

However the burden of persuasion might be allocated, it would undoubtedly be helpful if Congress adopted a more formal cost benefit analysis that would identify the gains, monetary or social, that a specific exemption would produce as well as the expected costs in both monetary and non-monetary terms. Moreover, this analysis should identify who will bear the costs and who will reap the benefits. For example, the current dairy pricing system imposes higher prices on milk used as fluid (bottled) milk. This means that low and moderate income families with

children are likely to bear a disproportionate share of the burden of supporting the dairy industry. There are other ways to ensure adequate income to diary farmers and guarantee that all regions of the country will have an adequate supply of milk that would distribute the costs differently. Unless such information is collected and analyzed, Congress will act without knowledge of the likely impact of its actions.

There are, at the same time, serious limits to a cost benefit analysis, however holistic, because it can not take account of the dynamics of the market. Inevitably, the market will respond to a change in the legal environment to the extent that the change has relevance to the actual operation of the market (some exemptions turn out in practice to be meaningless because the legislation rests on a total misperception of the problem and/or its solution). For this reason, *ex ante* cost benefit analyses can only make predictions about the future, but are very likely to miss significant costs or benefits that will only emerge over time. For this reason, a fully worked out system of critical evaluation should have an *ex post* review of the actual impact of an exemptive statute after a reasonable period of time–5 to 10 years. Such a review would allow comparison of the predicted costs and benefits with those that have actually resulted. This kind of *ex ante* and *ex post* review would be useful in terms of informing future legislative actions even if it were not linked to a sunset provision.

Two strategies, one judicial and one legislative, might facilitate a more rigorous approach to such statutes. Judge Easterbrook has said of exemptions:

> . . . [Such] legislation [is] a single-industry exception to a law designed for the protection of the public. When special interests claim that they have obtained favors from Congress, a court should ask to see the bill of sale. Special interest laws do not have "spirits," and it is inappropriate to extend them to achieve more of the objective the lobbyists wanted. . . . What the industry obtained, the courts enforce; what it did not obtain from the legislature–even if similar to something within the exception–a court should not bestow. . . . Recognition that special interest legislation enshrines results rather than principles is why courts read exceptions to the antitrust laws narrowly, with beady eyes and green eyeshades. *Chicago Professional Sports v. National Basketball Association*, 961 F.2d 667, 671-672 (7th Cir. 1992).

If courts adopted this approach and construed all exemptions against the beneficiaries, it could pressure Congress to be clearer in drafting such statutes and could restrict their more expansive interpretation. A study of the Local Government Antitrust Act has highlighted this problem. E. Thomas Sullivan, Antitrust Regulation of Land Use: Federalism's Triumph Over Competition, the Last Fifty Years, 3 *Wash. U.J.L & Pol'y*, 473 (2000).

Second, the AMC should consider recommending that Congress adopt a statutory rule of construction similar to that adopted in Wisconsin or Connecticut. The Wisconsin antitrust statute provides: "It is the intent of the legislature to make competition the fundamental economic policy of this state and, to that end, state regulatory agencies shall regard the public interest as requiring the preservation and promotion of the maximum level of competition in any regulated industry

consistent with the other public interest goals established by the legislature." Wi. Stat. 133.01. The Wisconsin Supreme Court has relied on this provision to impose strict limits on expansive claims to pre-empt competition. *American Medical Transport v. Curtis-Universal*, 154 W2d 135, 452 NW2d 575 (1990)(state antitrust law applies to an unauthorized ambulance service market allocation scheme adopted by the City of Milwaukee); see also, *Cedarhurst Air Charter v. Waukesha County*, 110 F. Supp. 2d 891 (E.D. Wis. 2000)(133.01 applied to reject state action immunity claim in a case involving airport authority exclusion of competition from the market for airport ground services).

Connecticut's legislature employed a different statutory strategy. Its statute declares: that the state's antitrust law will not apply only if the "activity is specifically directed or required by a statute of this state, or of the United States." Conn. G.S.A. sec. 35-31(b). The Connecticut Supreme Court recently relied on this provision to deny immunity to two municipal water utitlities that were accused of conspiring to monopolize the wholesale water supply in a region of that state. *Miller's Pond Co. v. City of New London*, 273 Conn. 786, 873 A.2d 965 (2005).

Adoption of either of these statutory standards would help to ensure that the federal courts in reviewing claims of exemption will employ Judge Easterbrook's standard.

Next, there is the question of whether there should be sunset provisions for exemptions. As a matter of theory, there should be. Antitrust decrees are now generally limited to 10 years or less exactly because of the recognition that the conditions of markets change over time.[1] Exemptive legislation like antitrust decrees should be reconsidered regularly. However, there are counter arguments against having a pervasive sunset requirement. Such a provision may make it easier for Congress to adopt such legislation on the pretense that it will be reconsidered in 5 or 10 years. In fact, it may be hard to get it removed from the books if it provides clear economic advantages to interest groups.

In looking at the statutes listed in the notice, some important distinctions exist. First, some exemptions are part of a program where an agency is charged with administering the market. But in other instances, the statute exists without connection to an agency. In the first instance, rather than a sunset provision as such, it is more important that the agency have a clearly defined goal of maximizing the role of the market and competition in the operation of the industry and so have the discretion to modify or terminate the exemption if it ceases to serve the public interest goals that Congress initially identified. Classic examples of such agency reform include the success of the Securities and Exchange Commission in eliminating fixed commission

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[1]As a young lawyer in the Antitrust Division, in the late 1960s, I had the task of reviewing a pervasive injunction governing the meat packing industry entered in 1920. That decree both governed and seriously inhibited the established firms. Sadly, my supervisors rejected even my modest suggestions for modification. The dead hand of the past continued to govern those firms well into the 1970s by which time many no longer existed and the rest had so declined that no rational basis existed to continue the decree.

rates for securities traders. The Federal Energy Regulatory Commission's successfully reorganized the natural gas industry, and its on going effort to reform electric power. The gas and electricity cases illustrate the problems that arise when the agency seeking to move toward a workably competitive market lacks full authority to revise the regulations governing markets to facilitate desirable competition. The better course in situations where agencies have on going authority to set the rules for a market is to give that agency the clear goal of limiting direct regulation while increasing reliance on market institutions as well as more authority to terminate or limit any exemption.[2] Finally, Congress should require the agency regularly to report on its efforts to minimize direct regulation by facilitating workable competition.

In contrast to exemptions that are part of an agency's regulatory process, other exemptions are free standing without any oversight of the operation of the exemption. For example, the recent medical resident matching exemption (15 USC 37b) assumes that the present system of matching will remain optimal for the indefinite future. Its premise is that neither resident programs nor medical school graduates seeking residencies will be able to manipulate the program in undesirable ways. Moreover, it assumes that this specific method of assigning medical residencies will remain the preferred method for the indefinite future. No agency has authority to oversee the matching program, modify its terms, or limit the scope of exemption in the event of changed circumstances.

The potential problem with these free-standing durable exemptions is that they may not serve the socially desirable goal that Congress imagined or with changed circumstances they may have created unintended, undesirable conseqeuences. Sunset provisions with a strict termination date requiring that both houses of Congress and the President must approve renewal might have more utility here. An alternative strategy worth considering would be to charge the Federal Trade Commission with overseeing all exemptions not expressly linked to an administrative agency, and conferring on the FTC the power to terminate the exemption after a period of years, e.g. 10 years, if it finds that the exemption has not or is no longer serving its stated goals. This would leave Congress with the opportunity to re-enact the exemption, perhaps in modified form. But any such legislation would require much more initiative from Congress than would be involved in simply renewing an exemption.

Another important distinction among the statutory exemptions listed in the notice is that some have continued relevance and others have no utility. It is important to remove the latter statutes from the U.S. Code. A number of exemptions on the AMC's list fall in this category

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[2] A further refinement would require that every transaction or activity for which the parties want an exemption should be notified to the agency and subject to review and express authorization. This is a feature of some, but not all, exemption provisions; it has the virtue of putting specifics out in public and allowing all stakeholders to have an opportunity to comment on the merits of the conduct to be exempted. This requirement can only operate where an agency has authority over the underlying industry and is given the power to grant or withhold the exemption.

including the Fishermen's Collective Marketing Act, the Anti-Hog-Cholera Serum and Hog-Cholera Virus Act, and Defense Production Act. Periodic review of some sort would ensure that these useless exemptions are removed from the books so that they can not be employed in some unintended way.

One last comment on the general question of statutory exemptions: Currently, statutory exemptions are scattered throughout the U.S. Code. There is no central listing of these provisions. The AMC is to be commended for collecting what may well be the first definitive list of such provisions. I would suggest that the AMC advocate that the revisor of statutes be instructed to collect all exemptions into a single place in the code or at least provide a comprehensive cross listing of exemptions. Such a listing would highlight the apparently random nature of the statutory process. More importantly, it would allow legislators wishing to propose exemptions to have ease access to examples of different exemptions with a variety of terms. For example the small business administration act exemption (15 USC 638(d), 640) provides an interesting dual review system as well as a system of termination for exemptions that no longer serve the public interest. Other exemptive statutes provide for time limited grants of exemptions that can only be extended after re-application to the granting authority.

2. *Comments on Specific Exemptions*

The AMC has asked for comments on eight specific statutory exemptions encompassing five industries (ocean shipping, agriculture, foreign trade, insurance, and commercial fishing). At the outset, it is notable that all of these statutes were originally adopted a number of years ago and accept for the Shipping Act have seen few amendments despite the dramatic changes in the industries involved. Most of the other anticompetitive regulatory statutes adopted over the period when these laws were first enacted have been repealed or the administrative agencies enforcing them have moved the industries toward less regulated, more competitive systems. Indeed, this has also occurred in the case of ocean shipping as well. Antiquity is not proof of irrelevance or undesirability, but it is very important to reconsider the merits of such regulation. Two of these areas, fishing and foreign trade, seem largely to have fallen into disuse. The remaining three exemptions have more continuing potential relevance to commerce.

a. Fishing and Foreign Trade

The commercial fishing exemption was largely construed out of existence in the 1950s and appears to be irrelevant. There have emerged, for reasons of resource conservation, other market organizing regulations that seek to limit competition to protect the fisheries. A recent study of that area is that of Professor Jonathan H. Adler, Conservation Through Collusion: Antitrust as an Obstacle to Marine Resource Conservation, 61 *Wash. & Lee L. Rev.* 1 (2004).

Based on the reported registrations shown on the FTC web site, it appears that very few American companies currently use the Webb-Pomerene Act provisions. Indeed, if the goal of collective action is to promote efficient global trade through joint ventures to market goods, then such conduct is lawful and needs no exemption. Only if competitors affirmatively seek to

exploit foreign markets by creating a cartel, would they require an exemption. Given the commitment of this country to global, competitive markets, it is bad international relations and bad substantive public policy to try to protect domestic cartels intended to exploit foreign markets. The limited use of these provisions suggests that they have little or no relevance to contemporary business. Their repeal would eliminate an embarrassing inconsistency in our law.

In short, these two exemptions can and should be repealed. They are statutes that no longer serve (if they ever did) the public interest.

b. Agriculture

There are two types of exemptions represented in the statutes: (1) those that provide some protections for farmer cooperatives as such (Capper-Volstead and sec. 6 of the Clayton Act) and (2) the Agricultural Marketing Agreement Act (AMAA) that authorizes government enforced cartels in the certain agricultural products.

It is my suggestion that farm cooperatives as such pose little threat to competition even when they seek primarily to act as pure bargaining agents for farmers (i.e., as a cartel manager). Absent the cartel protecting and empowering provisions of the AMAA, cooperatives have little power to control market prices. Several reasons combine to yield this result. First, the barriers to entry into the production of agricultural commodities are low. Hence, increased prices will and have called forth increased production as a result of both new entry and expanded output by existing producers. Second, a cooperative has different incentives than a conventional profit seeking monopoly. Specifically, a cooperative is usually committed to taking all that its members produce. Hence, it can not very effectively control output and raise prices above a market level. Moreover, even if it imposed limits on its members' production, members could and would resign and, in addition, new producers would enter the market thus overwhelming the efforts of even a monopolist cooperative to control price and output. It is true that some cooperatives have from time to time engaged in coercive and predatory practices in an effort to restrain production. However, such conduct is not shielded from antitrust scrutiny by Capper-Volstead. Two case studies of major cooperatives provide an empirical basis for the foregoing suggestion: Victoria Saker Woeste, *The Farmer's Benevolent Trust* (1998) (a history of the Sun Maid raisin cooperative showing that after it abandoned illegal coercive practices, it was unable to control the market for raisins until California created a state administered cartel upheld in *Parker v. Brown*, 317 US 341 (1943)); Willard F. Mueller, Peter G. Helmberger, Thomas W. Paterson, *The Sunkist Case A Study in Legal-Economic Analysis* (1987) (study of the California citrus cooperative that concludes that despite authority under the AMAA to regulate marketing, the cooperative was not able to control output or raise prices). In sum, while there are some troubling aspects of the Capper-Volstead Act, it has not and is unlikely in itself to create serious inefficiency.[3]

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[3] The current ability of cooperatives to merge and to form federations without apparent antitrust oversight (the merger issue is not entirely resolved as a matter of law) and without any

The AMAA on the other hand raises potentially more serious problems for efficiency because this act allows, with the approval of the secretary of agriculture, the creation of cartels that can invoke the authority of the United States government to suppress competition and raise prices. It appears that for the most part even these government authorized cartels lack significant market power because of the low barriers to entry into both producing agricultural commodities and their processing. However, in some instances, the powers conferred by the AMAA have been used to exploit downstream buyers or interfere with the efficient operation of the market. Last winter, the Florida tomato marketing order organization blocked the sale of a competing tomato that buyers sought because of its better flavor ostensibly because of the unattractive appearance of these tomotoes. Florence Fabricant, Forget About Taste, Florida Says, These Tomatoes Are Just Too Ugly to Ship, *New York Times*, A-13, December 21, 2004. This report illustrates the problems that the current order system can create. It should also be acknowledged that to the extent that the marketing orders provide quality certification and standardization that benefit both buyers and sellers, they may in fact facilitate efficient market operation rather than frustrate it. Thus, in general, the commodity order system should be modified to remove the ability of such organizations to exclude independent marketing of commodities. This would allow these organizations to continue to provide their market facilitating standard setting services without the risk of exclusionary conduct.

The most serious concerns with respect to market competition and efficiency arise in the dairy markets. Here the order system is most pervasive, serious issues of price manipulation by both buyers and sellers of milk and milk products exist, and some large cooperatives are allegedly exercising the powers conferred by the AMAA to exclude competition and attempt to control the market for fluid (bottled) milk. There is a significant body of scholarly literature debating the costs and benefits of this system. Without unduly prolonging this comment, among the important studies are: David Baumer, Robert Masson, Robin Masson, Curdling the Competition: An Economic and Legal Analysis of the Antitrust Exemption for Agriculture, 31 *Villanova L. Rev.* 183 (1986); Thomas L. Cox, Jean-Paul Chavas, An Interregional Analysis of Price Discrimination and Domestic Policy Reform in the U.S. Dairy Sector, 83 *Am J. Of Ag. Econ*. 89 (2001); and P. A. Ippolito, R. T. Masson, The Social Cost of Government Regulation of Milk, 10 *J. L. & Econ.* 33 (1978).

The fundamental problem is that the methods of protecting the economic interests of dairy farmers were developed long before long distance trucking of milk was feasible and so all milk was used for fluid or other purposes within the local market. It is undoubtedly long past time for Congress to rethink the way in which subsidies for dairy farmers should be collected and distributed. There are, indeed, a number of alternative ways to provide any desired subsidy without the kind of market distorting effects of the present system.

The AMC is not well positioned to propose a comprehensive plan for the reorganization

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public interest review by the Secretary of Agriculture are the most troublesome aspects of the current state of the antitrust exemption with respect to farmer cooperatives.

of dairy subsidies. It can, however, point out that the present system both insulates exclusionary and exploitative conduct from appropriate antitrust review and imposes significant costs on consumers that may yield little real gain to the purported beneficiaries–dairy farmers. The goal should be to encourage Congress to revisit the entire system of dairy pricing when it next considers major farm legislation.

c. The Shipping Act

This statute had its origins in a different era. Before the widespread use of containers for general cargo, there may have been some rational basis for a concern with destructive competition because the smallest unit for expanding capacity to serve a market was an entire ship Moreover, the rest of the world tended, historically, to favor cartels for shipping companies. As a result, the Shipping Act authorized American shipping companies to participate in "conferences" that set rates for service on particular routes. Today the Shipping Act is largely an anachronism that no longer serves well the public interest. The EU has recently issued a White Paper that is highly critical of the liner industry, and the OECD has also published a critical study. OECD Competition Policy in Liner Shipping Final Report DSTI/DOT(2002)2 (2002).

The most recent revisions of the Shipping Act authorized conference members to enter into contracts for rates other than conference rates and protected them from retaliation. As result, today, the vast bulk of general cargo moves outside the conference system at privately negotiated rates. The estimates are that as much as 80% or 90% of the cargo on major routes is now outside the conference system. There seems no justification to retain the general exemption for shipping companies that want to enter into cartels.

In examining this topic, it has seemed to me that shippers have two concerns that might be worth further consideration in the context of repealing the existing exemption. To the extent that the exemption system allows shipping companies to enter into legitimate joint ventures to share capacity and thus achieve efficiency without concern for antitrust liability, removing the exemption may increase some of the risks associated with such ventures. The other concern is with information sharing on the coordination of ship schedules. Both of these activities can, if legitimate, get business review clearances through the Justice Department. Although not the same as full exemptions, such clearances should provide significant reassurance that the proposed course of conduct is lawful. However, the AMC may want to consider whether the current procedures for considering and granting such reviews provide sufficient opportunity for other stake holders to have an effective voice in the review process and whether any need exists to reduce further any of residual risks of antitrust liability.

d. McCarran-Ferguson (Insurance)

This statute rests on a set of assumptions in dating from the mid-1940s about the negative implications of competition for the public interest in insurance that have long since been disproven. Although the antitrust exemption applies to the business of insurance generally, the real concern was to protect rate setting and policy term agreements in property and casualty insurance. It is now clear that rate setting agreements are not necessary to solvency and for most

lines of insurance in most states, competition has been the norm for some time. It is helpful to have common terms for policies, but this is a conventional regulatory process in which state action and the Noerr-Pennington doctrines provide insulation. Hence, the rationales for a broad antitrust exemption for insurance have long bee discredited.

There are some special considerations related to information pooling and analysis in the property and casualty insurance business that can raise antitrust concerns. There are both economies of scale and scope in pooling data on losses over extended periods of time and doing a consolidated analysis of that data to project trends for losses. The ABA more than 15 years ago (Resolution adopted at the 1989 Mid-Year Convention) recommended elimination of the general exemption but also suggested that the law continue to provide a safe harbor for legitimate and reasonable information pooling and analysis that served the public interest. Nothing in the intervening years makes that recommendation any less relevant today.