

July 27, 2006

Honorable Arlen Specter
Chairman
Committee on the Judiciary
United States Senate
224 Dirksen Senate Office Building
Washington, DC 20510-6275

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Attn: Barr Huefner

Re: The McCarran-Ferguson Act Additional Comments

Dear Chairman Specter:

Thank you for the opportunity to provide testimony on behalf of the American Bar Association on the Committee's review of the McCarran-Ferguson Act on June 20, 2006. I am responding to the additional questions from you and Ranking Member Leahy, and I appreciate the additional time you allowed me to respond.

Question of Senator Arlen Specter: Please provide the Committee, to the best of your ability, with examples of cases in which states took no action to prosecute conduct by insurance companies that would have constituted a violation of the federal antitrust laws, or where their actions were limited because antitrust law could not be applied.

After considerable review of our resources, we cannot point to specific cases that were not brought by the states that would constitute a violation of the federal antitrust laws. That would require a major survey, and, even with considerable research, would be very difficult to establish. We can, however, establish that many of the states would not pursue antitrust actions against the insurance industry for the same reason that the federal government did not pursue them – because many states also have exemptions to the antitrust laws similar or identical to McCarran-Ferguson. Several states, notably Florida and Massachusetts, incorporate all federal exemptions to the antitrust laws into their state antitrust laws. Other states, notably Illinois and New Jersey, expressly provide that their state antitrust laws are to be interpreted consistent with federal law. At least fifteen other states have express state antitrust law exemptions for the insurance industry written into their laws. A large number of states, therefore, would not bring state antitrust actions against insurance companies because they would face the same difficulty in prosecuting their cases as the federal government faces today – the anticompetitive conduct of the industry is exempt. If McCarran-Ferguson were repealed, the states that provide the same exemptions as the federal government or follow federal precedent would be able to pursue antitrust actions against insurance

companies under their state law. The states with express exemptions would still maintain their exemptions unless they expressly repealed them (and there may be support for such repeal arising out of the Congressional repeal of McCarran-Ferguson).

The other issue that is relevant to this point is that the range of penalties and remedies under the federal antitrust laws is clearly broader and more potent than any state law penalty or remedy could be. While the record of prosecutions and recoveries that New York State has achieved in its recent cases, as outlined in Ms. Hoffmann's testimony to the Committee, is impressive, the antitrust claims are brought under the Donnelly Act, not the Sherman Act, and are thus limited. New York's action against Aon Corporation included settlements with Illinois, and Connecticut, but not a settlement broadly covering the United States, as would be possible under the Sherman Act. If actions for bid rigging and rate fixing were prosecuted criminally under the federal antitrust laws, the corporate maximum fine is \$100 million and the maximum individual sentence is ten years in prison. These are penalties that would be substantially higher than any state antitrust penalties. Similarly, federal private damage actions under Section 4 of the Clayton Act would permit treble damage recoveries for alleged conspiracies on a national basis. The deterrent impact of federal enforcement would be substantially enhanced if the exemption were repealed.

Questions of Senator Patrick Leahy:

- 1. The ABA recommends repeal of the McCarran-Ferguson insurers' exemption, but also the continued regulation of insurers by the States. If Federal antitrust laws were to apply to the business of insurance, how would current State antitrust laws and any applicable State exemptions be affected?*
- 2. Would Federal antitrust law preempt all inconsistent State antitrust law?*
- 3. Could a Federal body of antitrust law applicable to the business of insurance coexist with 50 separate bodies of State law?*
- 4. Do you foresee tension between Federal enforcers acting under Federal antitrust laws, and State regulators and attorneys general whose State antitrust law might contain an exemption for insurers?*
- 5. Do you have any recommendations as to how a State regulatory system and an applicable body of Federal antitrust law could coexist?*

I believe these questions can best be answered together. If the federal antitrust laws applied to the business of insurance, the federal and state antitrust laws would operate as they operate with respect to all businesses that are not subject to an exemption. In our experience, criminal prosecutions and major cases seeking injunctive relief generally are brought at the federal level. The states may sometimes join in the federal civil actions, or bring their own actions, as appropriate. Where states have existing exemptions for the business of insurance, those states with exemptions that flow from the federal law will no longer have exemptions. Those that have express state law exemptions will either maintain those exemptions or reconsider them in light of the new federal law. If they maintain them, they will simply be precluded from bringing antitrust actions under state law against insurance entities.

Honorable Arlen Specter
July 27, 2006
Page 3

On the issue of preemption, if McCarran-Ferguson were repealed and insurers were subject to the federal antitrust laws, the federal law would not preempt all inconsistent state antitrust laws. That was made clear by the U.S. Supreme Court in *California v. ARC America*, 490 U.S. 93 (1989) with respect to state indirect purchaser statutes that are at odds with the federal law. Preemption occurs only where (1) Congress expressly preempts by statute; (2) there is a congressional manifestation of the intent to “occupy the field”; and (3) an actual conflict exists between the federal and state law. *Crosby v. National Foreign Trade Council*, 530 U.S. 363 (2000). Indeed, in the antitrust world today, the indirect purchaser statutes of many different states demonstrate that federal and state antitrust laws allowing for very different damage recoveries are able to coexist.

The “safe harbors” provisions discussed in my testimony on behalf of the ABA is an effort to allow the state regulatory process to operate in areas such as the collection and dissemination of past loss experience, standardized policy forms, joint underwriting agreements and residual market mechanisms subject to the active supervision of the state commission. All other matters are subject to the federal antitrust laws. This provides a means to address necessary regulatory activity in a manner consistent with the operation of the federal antitrust laws.

A final point is that the recent proposals for federal chartering of insurance companies have proposed that federally chartered insurers would not be subject to state regulation and would be subject to the federal antitrust laws. While taking no position on these proposed bills, federal chartering raises some additional issues for consideration in this discussion.

I hope that these responses are helpful to the Committee in its continuing consideration of the repeal of McCarran-Ferguson. The American Bar Association remains available to assist the Committee on this important issue.

With best wishes,

Yours faithfully,

A handwritten signature in black ink that reads "Donald C. Klarner". The signature is written in a cursive style with a long horizontal flourish extending to the left.

Chair, Section of Antitrust Law

cc. Lillian Gaskin, Senior Legislative Counsel